

**SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS**

January 1992

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SUMMARY*

Reports by business and banking sources contacted by Federal Reserve districts suggest that activity was lackluster as the year drew to a close. Retailers in most districts report that holiday sales were at or modestly above year-ago levels before adjustment for price changes. Manufacturing sources generally note steady or declining production and employment. Except for export goods, orders and backlogs generally softened into 1992. According to realtors, lower mortgage rates have aided home sales, particularly of lower-priced properties. Single-family construction expanded modestly, while new commercial activity remained dormant. Aside from a surge in mortgage refinancing, banking sources suggest that consumer and business loan demand has not revived. Bankers report no change in credit standards. While some bank contacts report ongoing loan quality problems, others are optimistic about prospects for improvement as borrowers work down debt service burdens. Energy industry contacts confirm that lower oil and natural gas prices are leading to cuts in expenditures for drilling and energy-related products. District reports indicate that commodity and materials prices were generally unchanged or declining; pressures on wages and retail prices have been minimal. Despite softness as the new year began, business and banking contacts generally anticipate that economic conditions will improve by mid-year.

*Prepared at the Federal Reserve Bank of Atlanta and based on information collected before January 13, 1992. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

CONSUMER SPENDING

Retailers generally confirmed that holiday sales were flat to slightly higher than year-ago levels before adjustment for inflation. Discounters and some specialty stores posted better performance at the expense of traditional department stores. Sources in Atlanta, Cleveland, Kansas City, Minneapolis, and Dallas report modest sales gains led by nondurable goods, particularly basic apparel and other small-ticket items. Sales in several districts were below expectations, and retailers in the Philadelphia district have continued to cut prices through early January.

Inventories held by retailers in Chicago, Cleveland, Dallas, and Philadelphia were above target levels in early January, while retailers in Atlanta, New York, and Kansas City were content with current inventories. Retail contacts generally do not plan to expand stocks aggressively in the first quarter.

According to auto dealers, new car sales were generally weak in Atlanta, Chicago, Dallas, Kansas City, and San Francisco districts. However, Minneapolis and Cleveland report some improvement in auto and truck sales.

Retailers and auto dealers generally expect sales to recover in 1992, but not until the second half of the year. Strict inventory control, competitive pricing, and continued cost-cutting were cited by several districts as the general strategy for the near future.

MANUFACTURING

Factory activity faltered in most districts through early 1992 according to those surveyed. Renewed weakness in production and orders was cited by most contacts. Dallas contacts report that chemical production is flat and demand for oil field machinery is declining with oil prices.

Weak auto output has hurt auto suppliers, according to Cleveland and Atlanta. Chicago also cites continued weakness in auto production and few signs of a turnaround in orders for appliances, heavy equipment, or primary metals.

St. Louis and Atlanta report stable or increasing demand for packaging materials, where some price increases are sticking. Export demand continues to rise for some firms, according to sources in Kansas City, Boston, Richmond, and St. Louis. Manufacturers in Philadelphia report steady industrial output.

Boston contacts indicate that capital spending is restrained by adequate or excess capacity and concerns about debt. Cleveland sources confirm that capital goods orders recently declined. Plants are generally operating below capacity, according to industry contacts in Kansas City, and Dallas chemical producers are concerned about overcapacity. Several districts report that, despite recent reductions in interest rates, capital expenditures will remain at 1991 levels until economic conditions improve, although there were several reports of productivity-enhancing capital projects.

Kansas City, Philadelphia, Atlanta, and Richmond report generally stable prices for material inputs and products. Factory product prices are flat in the Boston district; the weakest lines are being discounted.

Inventories in the Kansas City and Philadelphia districts continue to drift downward, though no district reports excessive inventories as a major problem. Plans to expand stocks are conspicuously absent. Manufacturers' general expectations for the first quarter are for continued weak sales and flat prices, but sources are relatively uniform in expecting significant improvement in sales and production in the second half of 1992.

REAL ESTATE AND CONSTRUCTION

Realtors in most regions report that lower mortgage rates have prompted modest gains in home sales. In Atlanta and New York, real estate contacts note that a significant portion of the home sales originated with first-time buyers and lower-priced properties. Sales in the Boston and Richmond districts remained mostly flat over the past six weeks. Except in the San Francisco district, which reports some continued decline, sources in most areas find home prices to be relatively stable.

Reports from St. Louis, Kansas City, Dallas, and Atlanta note some improvement in single-family starts, but starts in the New York district remain slow due to generally sluggish demand. Multifamily activity remains stalled in Atlanta but is accelerating in Dallas.

Realtors, mortgage lenders and home builders are generally optimistic for the spring. Bankers in Philadelphia, Cleveland, and Kansas City believe residential mortgage activity could post healthy gains. Atlanta realtors expect strengthening sales and St. Louis builders believe that conditions will improve significantly by mid-1992.

In the Dallas district, industrial and office real estate demand is flat. Office leasing declined in the New York area since the last report. Commercial activity in the Minneapolis district is mixed. Dallas and St. Louis report moderate increases in public construction.

BANKING AND FINANCE

Aside from a surge in mortgage refinancing, most districts report consumer and business loan demand has not expanded significantly. Contacts in several districts say that households are refinancing from adjustable-rate to fixed-rate mortgages. San Francisco also suggested that savings from lower monthly payments are being used for household debt reduction. Gains in

new mortgage activity are much spottier. Demand for other consumer and business loans was generally reported flat or down.

Reports on loan quality were mixed. New York contacts report increased delinquency rates on all types of loans, forcing some restructuring. San Francisco found that bank profits are still restrained by deteriorating real estate loans. Philadelphia bankers expect improving portfolio quality as lower interest rates reduce debt service costs. Bankers in Atlanta noted either stabilization or improvement in the quality of their portfolios during the fourth quarter.

Credit standards, on balance, remain unchanged. The consensus among banking contacts is that aggregate loan demand will remain flat until the second or third quarter of 1992.

AGRICULTURE AND NATURAL RESOURCES

Winter crops are generally said to be in good condition across the nation with the exception of the Dallas district, which reported severe weather damage to agricultural production. Livestock producers in several districts are struggling with lower prices.

Declining oil and gas prices have resulted in reduced drilling activity in the Kansas City and Dallas districts. Dallas reported that lower prices are creating a somber energy outlook for 1992 and added that some producers are shifting exploration overseas, while many energy and related companies have announced layoffs.

FIRST DISTRICT-BOSTON

Economic activity continues at a low level in the First District. For most retailers, Christmas sales were even with last year's. Manufacturing demand remains weak, with sales and orders below year-ago levels at most firms contacted. Manufacturers' employment continues to decline, and capital spending plans are restrained. Few firms expect any improvement before mid-year.

Retail

Nominal dollar sales were level with Christmas 1990 for the majority of First District retailers contacted in early January. The few merchants who reported significant increases over last year are upscale or specialty stores. For virtually all retailers, consumer activity was particularly restrained in the first half of the Christmas season, but a later-than-usual "last minute rush" prevented major sales declines.

Although some retailers offered large discounts early in the season, prices have now stabilized. A few merchants with especially strong market positions passed some cost increases on to consumers. Most continue to maintain strict control over inventory. In general, both margins and profits are flat.

All contacts undertook routine seasonal hiring, but plan no changes in permanent employment. Wage increases are minimal. With few exceptions, capital spending plans are severely limited. Preserving liquidity reportedly has priority over large investment commitments since consumer spending remains erratic and competition intense. Few foresee a substantial improvement in their business in the new year.

Manufacturing

First District manufacturing conditions remain sluggish. A majority of respondents indicate that late 1991 shipments were down from year-earlier levels, with reported declines ranging from 4 to 20 percent. Several contacts experienced renewed weakness in the fourth quarter, with new orders and backlogs below late 1990 levels. Only a small minority saw modest year-over-year gains. Still, despite generally weak demand, most contacts pointed to at least one product line with rising sales and orders. Some electronics and telecommunications products were relatively strong, as were sales by some companies to the health care sector, brokerage firms, and customers in aerospace, plastics, and environmental protection. Although the auto industry is expected to be weak over the medium term, two contacts reported increased sales to U.S. auto firms and to Japanese transplants. The European and Canadian economies were generally said to be as weak as or weaker than the U.S. economy, but a few firms reported a rise in foreign sales.

Manufacturers' sales prices are generally flat to down. Most contacts are offering discounts on their weakest lines or across the board. In turn, respondents are seeking price concessions from their own suppliers. Still, several report pinched margins, only partially relieved by productivity gains. To contain costs, two-thirds of the respondents have reduced employment from year-ago levels, either through layoffs or attrition. Almost half are planning or considering further cuts. No firm expects to expand its work force any time soon.

One-third of the respondents plan to increase capital spending in 1992 by as much as 10 percent. For the rest, investment will be equal to or less than year-ago efforts. In explaining their restrained

investment plans, almost half point out that they have adequate or excess capacity. Others mention concerns about cash flow or onerous debt levels. While lower interest rates reduce the cost of carrying this debt, no contact indicates that interest rate cuts will lead his firm to make additional investments in the near term. A few contacts hope that such cuts will prompt their customers to do so, however.

A majority of manufacturing contacts expect no improvement in economic activity before the second half of 1992. A few hope for a pickup in the third quarter in response to lower interest rates; others express faith in election-year fiscal initiatives. Even so, most expect very slow growth over the medium term.

Residential Real Estate

Reports on First District home sales vary. Some realtors report that sales have picked up to relatively healthy levels; others say sales remain weak. Even where home sales are low, no additional weakening has occurred in recent months. Moreover, realtors contacted think home prices have bottomed out or are close to doing so.

Outlook

The nonprofit New England Economic Project (NEEP) released its semi-annual forecast in early December. Based on a forecast that the national economy would "continue to creep sluggishly out of recession," the NEEP forecasts call for a delayed recovery in New England, with total nonfarm jobs showing no growth until the third quarter of 1992. Manufacturing employment losses will continue until the end of 1992 for the region as a whole, while nonmanufacturing shows some growth as early as the second quarter, notably in wholesale and retail trade.

SECOND DISTRICT--NEW YORK

Developments in the Second District economy since the last report were generally on the soft side. During November retail contacts were split between those with sales above and below plan while December results were generally below target. Residential construction activity remains low and office leasing activity slowed. District unemployment rates rose in December for the third consecutive month following a seesaw pattern during most of the year. Most senior loan officers at small and midsized banks reported no change in their willingness to lend.

Consumer Sector

District retail contacts had mixed results during November, splitting almost evenly between those with sales above and those with sales below plan. While December results were more uniformly below target, several retailers expressed pleasure that sales proved better than the dire media forecasts. The sales environment was very competitive and marked by considerable price-cutting which began very early in the holiday season. Despite relatively lean inventories, retailers were heavily promotional in an attempt to overcome anticipated consumer caution. Over-the-year sales changes at department stores ranged from -4 percent to +5 percent in November and from flat to +2 percent in December. An annual survey conducted by the Retail Council of New York State covering some 200 stores across the state found sales volume during the Christmas season to be generally unchanged from a year earlier.

Items which sold relatively well included staples such as men's and women's sweaters, gloves, and outerwear as well as dresses, cosmetics and certain toys. Sales of big ticket items varied among respondents. Due in large part to a substantial pickup in sales during the two weeks surrounding Christmas, inventories were reported at or somewhat below targeted levels.

Residential Construction and Real Estate

Residential construction activity remains slow in the District due to both the season and generally sluggish demand. The high inventory of homes available in the resale market and consumer uncertainty about the economic outlook continue to be cited as major factors. Reportedly, much of the homebuying which is currently taking place is by first-time buyers and others in need of "affordable", lower-priced units. Two yet-to be-constructed communities in New Jersey and New York were recent sellouts because of their relatively low prices and attractive financing. Among other housing construction scheduled are an \$18 million building in the Bronx to house homeless adults and, in all five boroughs of New York City, new housing for working and middle-class families under a recent \$76 million federal grant.

Office leasing activity slowed somewhat since the last report. Midtown Manhattan witnessed its second largest transaction of the year, but a sizable amount of vacant space was marketed and the primary vacancy rate rose. In downtown Manhattan, where no new construction is underway and several well-known buildings are undergoing extensive capital improvement, the vacancy rate declined for the second consecutive month.

Other Business Activity

District unemployment rates rose in December for the third consecutive month following a seesaw pattern during most of the year. New York's rate edged up to 8.1 percent from 8.0 percent in November while New Jersey's rate increased to 7.4 percent from 7.1 percent. Since the last report, plans for some sizable cutbacks have been announced which are likely to have a downward impact on local employment. Nynex, the local telephone company in New York State and New England, will reduce its workforce over the next two years by almost 10,000 and Xerox, which has several locations in the District, will eliminate 2500 white-collar positions by the middle of this year. Moreover, in the semiannual survey of the Manufacturers Association of Central New

York, nearly 25 percent of respondents in January said they plan to cut employment over the next three months, up from 15 percent last July.

On a more positive note, Ford and GM recently announced plans to invest a total of \$350 million in their western New York plants over the next two years. Most of the money will be used for new machinery and retooling. In addition, a Dallas-based firm plans to move a manufacturing operation from the South to New York State.

The December survey of Buffalo purchasing managers showed a doubling of the percentage of firms with fewer new orders and a substantial increase in the percentage with lower production. While some of this slowdown apparently is a seasonal pattern, the extent of it is somewhat greater than in December 1990. The November survey of purchasing managers in Rochester, however, showed a decline in the percentage anticipating a deterioration of business conditions over the next quarter.

Financial Developments

Most senior loan officers surveyed at small and midsized banks in the Second District reported that their willingness to lend remains unchanged from three months ago. Credit standards at most banks surveyed remain the same, though a few banks reported stricter standards for consumer loans. Most respondents stated that overall loan demand was stable with some variation across categories. Nearly all loan officers reported charging lower rates than three months ago, reflecting decreases in the prime rate. These lower rates have brought about increased demand for mortgage refinancings, even though the demand for new residential mortgages and construction loans remains weak. Those respondents noting a decrease in overall loan demand are using advertising campaigns and aggressive rate-cutting policies as a way of attracting new loans. The majority of banks surveyed report an increase in delinquency rates on all types of loans, forcing some to restructure existing loans.

THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District appeared to be steady in late December and early January, based on reports from major business sectors. Manufacturers generally indicated that business was steady although some firms were trimming working hours. For most retailers, Christmas season sales were even with the prior year in current dollars. This was below expectations, and many stores were holding special January sales to reduce inventories. Bankers reported that loan demand remained essentially flat except for a surge in mortgage refinancing applications in recent weeks as interest rates fell.

Third District business contacts generally foresee some improvement later in the year. Manufacturers expect the pace of orders to pick up over the next six months. On balance, they are planning to add to payrolls and boost capital spending by midyear. Retailers anticipate a somewhat better sales picture, but not before the third quarter. Bankers are also looking to the second half for improvement; they expect a modest upturn in business and consumer lending to get underway then, although some believe residential mortgage activity could post healthy gains this spring with an increase in home sales.

MANUFACTURING

Reports from Third District manufacturers in early January were mixed, but on balance suggested that industrial activity was running at a steady pace. While shipments were moving up, area firms indicated that new orders were being received at just a level rate. Manufacturers gave mixed reports on inventories although it appeared that, on net, stocks were edging down. While employment was practically steady, according to a majority of companies contacted, one-fourth noted recent reductions in working hours. Nearly all manufacturers said prices for both inputs and the products they make were holding steady.

Looking ahead, about three-fourths of manufacturers contacted for this report expect business to improve by midyear, and the rest were about evenly divided between those

anticipating steady business and those expecting a decline. Overall, manufacturers look for an increase in orders to boost backlogs and lead to some further reduction in inventories over the next six months. In line with this forecast, industrial firms in the Third District are planning to extend working hours and increase payrolls slightly. They are also scheduling some increases in capital spending for the first half of the year.

RETAIL

Most Third District retailers contacted for this report indicated that sales for the Christmas season were below their expectations. On average, sales were approximately even with 1990 in current dollar terms. Mass merchandisers and department stores generally saw sales slip marginally from 1990 levels while discounters and some specialty stores (especially mid-priced jewelry and apparel stores) posted gains. Nearly all types of stores were making further price cuts on a broad range of goods in January to reduce excessive inventories, and most merchants said that the pace of sales in the first week of the month was fairly steady. Store officials generally expect January sales to exceed the low levels of January 1991, but most expect the current November-January fiscal quarter results to just match the year-ago period in current dollars.

Most retailers expect sales to remain slow at least until midyear. They hope that improving overall economic activity by that time will boost consumer confidence and lead to healthier sales. Nevertheless, many retail contacts do not expect a strong upward trend in consumption spending to develop. Expecting little short-term improvement in demand, and concerned that competitive pressures due to over-capacity will continue, store executives do not anticipate significant increases in revenues. Instead, many indicate they will be looking to improve operating efficiencies in order to bolster profit margins.

FINANCE

Most Third District bankers contacted in early January said loan demand remained soft except for a surge in applications for mortgage refinancings. Although there were a few reports of slight upturns in home purchase mortgages, mainly for lower-priced homes, real estate loans outstanding at major banks in the Third District continued to trend down. Bankers

also described demand for consumer installment credit as flat to slightly down in recent weeks. Bankers generally reported a similar trend for commercial and industrial loans.

On the whole, Third District bankers expect a gradual improvement in the economy and a slow pickup in lending to get underway around midyear. Bank lending officers said the recent decrease in interest rates will make debt service more manageable for business borrowers with floating-rate loans, leading to some improvement in credit quality for both current and potential borrowers; but bank lending officers generally do not expect the lower rates to prompt a significant upturn in demand for commercial and industrial credit. Some bankers said they expect increased homes sales in the spring to boost mortgage demand.

FOURTH DISTRICT - CLEVELAND

Summary. There is still little sign of a renewed recovery in the Fourth District. Major retailers experienced a sales gain during the Christmas season from levels a year earlier, but the increases were less than expected. Industrial activity in the District slowed recently, led especially by the auto industry. Revived growth in industrial production could occur this quarter, if auto production strengthens as generally expected. Lower interest rates have boosted refinancing of mortgage and business loans, but new business and consumer lending still shows little indication of growth.

Consumer Spending. Retail sales during the Christmas season were reported between 2% and 4% above levels a year earlier. A few retailers cited better-than-expected sales, but others described sales as disappointing or "below plan". Sales in a large upscale shopping center were said to be better than in 1990, but ranged widely between retailers who posted large gains and those who had declines from a year earlier. A retailer with stores throughout the District reported that sales in Cleveland, Pittsburgh, and Cincinnati were stronger than nationally and than a year ago, but sales in some smaller metropolitan centers of the District were weak. Despite the uncertain outlook going into the holiday shopping season, price discounting was no greater than a year earlier, according to some retailers.

At year-end 1991, inventories were larger than desired by some retailers. They generally have shaved their sales goals for the spring months, but uniformly expect a stronger second half than first half of 1992.

According to economists associated with consumer goods industries, real consumer spending last quarter rose between zero and a 1% annual rate, and is expected to rise between a 1% and 2% annual rate this quarter. There is little support among them for a temporary cut in personal income taxes to stimulate spending.

Automotive. Most automotive analysts anticipate that the auto industry will contribute to growth of industrial production and total output this quarter, following a decline in auto output last quarter. Auto production is expected to increase a few percent this quarter from last. Industry analysts do not expect additional production layoffs this quarter, although temporary plant shutdowns could occur if inventories rise more than desired. New car stocks are said to be larger than desired for some cars, but low for a few popular models.

Auto dealers in the District are a little more optimistic about short-term sales prospects than they have been in recent months, because their December sales improved from November and from a year earlier. That helped to cut some of their excess inventories, and most dealers contacted now expect that they will slightly increase their factory orders this quarter from last.

Manufacturing Conditions. Weakened automotive output has set back auto-supplying industries. Steel producers note a letup in orders for delivery during the rest of this quarter, and consequently a shortening in lead times.

Also, some cutback in steel inventories this quarter, following a larger-than-desired buildup last quarter, will likely result in a trimming of steel output. Orders for auto paints and coatings and glass have softened since last fall, but are no longer deteriorating, according to a major supplier. Some auto tire analysts expect that both original equipment and replacement tire demand in 1992 will be up a few percent from 1991, but no pickup from the present weak demand is expected until after the first quarter.

Several capital goods producers report a softening in orders in the past month or two following a revival that began last spring. The upturn in heavy-duty truck output flattened in recent months after several months of irregular but rising activity, according to a supplier. The daily average of orders for an industrial equipment producer in December fell after a steady climb through November. Customer inventories are believed to be low, however, because orders have been more frequent but smaller. A parts supplier to the office machinery industry reported a further rise in orders through last quarter. He expects that spending for real producers' durable equipment last quarter rose at about a 5% annual rate, led by the computer and aerospace industries, with most other capital goods industries showing little change from the previous quarter.

Manufacturers in general do not anticipate an increase in their capital spending in 1992 from 1991, although spending plans vary widely by industry. Some producers expect higher outlays this year, particularly for equipment, to improve product quality, broaden product lines, and increase productivity. Some plan less spending this year than last because of cutbacks in business

structures. A tool producer plans a step-up in spending this year for further modernization of existing facilities. Although the primary metals industry is apparently anticipating some cutback in spending this year, a producer plans a large capital expenditure for quality and cost improvement. A mineral resources producer expects his firm and industry to cut back spending in 1992 because of prospects for weak prices for their products.

Capital spending plans are not being delayed, although some may be stretched out, and discussion of a possible tax change is not yet affecting spending plans. A common view among manufacturers seems to be that an investment tax credit, although less beneficial over the long run than a cut in corporate tax rates, would be a temporary stimulus to investment.

Financial Developments. There is still little sign of strengthening in new business or consumer loans, according to banks and thrift institutions. Lenders report, however, heavy demand for refinancing of mortgage loans, and more businesses are refinancing bank loans. Some lenders have only recently begun to lower borrowing rates on consumer installment loans, but interest rates on a 30-year fixed-rate loan have been easing steadily and are now common at 8%, with some mortgage bankers offering rates at about 7.5% plus points. Many mortgage lenders anticipate a sharp rise in demand for new loans during the spring. Some thrifts report that mortgage holders are shifting from adjustable-rate to fixed-rate mortgages.

FIFTH DISTRICT-RICHMOND

Overview

District economic activity was mixed in late December and early January, while confidence about the economic outlook rose. Retail sales were generally flat. Manufacturing activity declined, compared with stable activity in the previous survey. Both retailers and manufacturers, though, were more optimistic about their prospects over the next six months than they had been in the last survey. Lower mortgage rates lifted home sales in some areas and spurred refinancing activity and inquiries by prospective homebuyers throughout most of the District. Exports rose faster than imports at District seaports, and farmers began the new year with generally favorable weather and price conditions and improved balance sheets. State revenues were mostly on target, although some further expenditure cuts were expected in coming months.

Consumer Spending

Our regular mail survey indicated that District retail activity stabilized in December after several months of decline. Survey respondents said that sales, adjusted for seasonal factors, remained steady after November and that shopper traffic improved. Inventories, employment, and capital expenditures fell. Retail prices were stable, while wholesale prices and wages rose.

Retailers were optimistic about sales and shopper traffic over the next six months. They expected wages, wholesale prices, and retail prices to rise and employment to fall further.

Manufacturing

Our survey of manufacturers indicated that District factory activity

declined in recent weeks. By comparison, activity had been stable in the previous survey. Respondents reported decreases in most indicators. Exports increased, however, and little change was reported in prices or capital expenditures.

Manufacturers' forecasts for the coming months were more optimistic than in the previous survey. They expected increases in all measures of economic activity except inventories, which they thought would be stable. Two-fifths of the respondents expected increases in manufacturing employment and total employment in their respective states.

Ports

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated that exports were generally higher in December than in November, while imports were unchanged. Compared with a year ago, export activity was higher and import activity was lower. Exports were expected to increase faster than imports during the next six months.

Finance

District financial institutions contacted by telephone indicated that credit standards were unchanged over the last six weeks. Although some banks noticed a slight increase in consumer and commercial loans, most reported that demand was flat over the period. All of the banks contacted had lowered their prime rates during the last six weeks, and almost all had reduced loan rates across the board. Lower interest rates, respondents said, have accelerated refinancings, which constituted a substantial majority of home mortgage requests.

Housing

Real estate analysts, homebuilders and mortgage bankers surveyed by

telephone reported that the residential market remained mostly flat over the past six weeks. Some respondents, though, suggested that sales in their areas were beginning to increase. Many noted that lower mortgage rates had increased traffic and that home prices were steady. In areas where sales remained sluggish, potential homebuyers were insecure about their jobs and income levels.

State Budgets

A telephone survey of state government forecasters indicated that revenues were mostly on target, except for a moderate shortfall in South Carolina. In contrast, the states experienced large shortfalls last year. This year's forecasts assumed more modest economic growth than did last year's. In several jurisdictions, December revenues from specific taxes were unusually strong, but forecasters were unsure of the reasons. Generally, tax revenues were still depressed by sluggish economic growth.

North Carolina reportedly had no need for further expenditure cuts, and it was unclear whether South Carolina would have to trim its budget. Other Fifth District jurisdictions were considering major spending cuts, and several were considering tax increases. Several respondents said that rapid growth of federally mandated Medicaid spending continued to be a primary source of budgetary pressure. State government worker layoffs were considered likely in Virginia, Maryland, and the District of Columbia. In West Virginia, cuts were expected to trim state agencies' material and travel budgets.

Agriculture

Farm analysts indicated that conditions in agriculture improved in recent weeks. Rain relieved dry conditions in most of the District and left the small grain crop in generally good condition. Hog prices, already below

levels of a year ago, fell further in recent weeks; otherwise, most livestock prices were at or above year-ago levels. District farmers entered 1992 with a stronger financial position, thanks to relatively good 1991 crop yields and strong livestock prices.

SIXTH DISTRICT - ATLANTA

Overview: Contacts in the District reported that economic activity in December was generally sluggish. Retailers saw disappointing Christmas sales that were even with to modestly above year-ago levels. Discounters benefitted from increasing demand from price conscious consumers, taking market share from department stores and upscale shops. Auto sales showed no signs of improvement. Manufacturing activity remained slow, although firms in the printing and packaging industries reported modest increases in orders and production. Banking contacts report that loan demand was again flat. Home sales in the lower price ranges continued to show improvement, and realtors are optimistic for spring sales. Commercial construction, however, remained dormant. No exceptional wage or price pressures were reported.

Consumer Spending: With the exception of discounters, retailers contacted throughout the District reported that, in real terms, Christmas sales were even with year-ago levels. Discounters consistently outperformed department stores and reported sales gains over last year. The largest gains were noted in sales of "basics," not luxury goods, and were led by apparel items. Customers paid with cash more often than in previous years. Inventories remained lean but reportedly did not constrain holiday sales. Retailers do not anticipate significantly increasing new orders in the near future and are not optimistic about first quarter sales. Durable goods sales have not improved; automobiles and household appliances are particularly soft. While Florida contacts report increasing numbers of foreign tourists, this growth has not been sufficient to offset declines in domestic traffic. Per capita visitor spending is also down from a year ago.

Manufacturing: Few manufacturers in the region report increasing activity. Stagnant commercial construction continues to impact carpet producers adversely. Weakness in the furniture and auto markets is holding back textile production. While apparel producers note that demand for some lines, particularly athletic wear and denim products, is expected to continue

to post good growth, new orders for other lines have been weak. Military contractors continue to report declining orders and employment because of defense spending cuts. Low steel prices and slack consumer spending on big ticket items are hurting a regional producer of steel for appliances.

More positively, contacts said that employment remained stable and that orders have increased for producers of printed materials for business and for packaging of consumer products. Sales picked up in the fourth quarter for a large paper producer and recent product price increases appear to be sticking according to a company spokesman. Lumber and wood industry contacts expect demand to pickup sharply over the next few months as housing starts begin to improve.

Financial Services: The majority of bank contacts in the region reported that loan demand was flat in December and remained below year-ago levels. Several bankers expressed disappointment with the limited amount of new loan activity that has emerged since the recent reduction in interest rates. However, one contact did note that the drop in rates had sparked some optimism in the local business community. Lower rates have also resulted in a wave of mortgage refinancings.

Most bank contacts report that the quality of their loan portfolios either stabilized or improved slightly in the fourth quarter. They added that their credit standards were essentially unchanged in the last six weeks. Auto dealers and construction contractors continue to report that credit is tight.

Construction: After adjusting for seasonal variations, most realtors reported improved December home sales compared to activity in recent months. The strongest sales are again in the lower to mid-price ranges as first-time buyers continue to be drawn into the market by lower mortgage interest rates. The luxury market is "quiet" and sizable price concessions are being

made, according to most brokers. Several noted that people who are currently renting are now finding it possible to buy a home with comparable after tax payments. Most realtors expect continued sales gains and are optimistic for the spring. Single-family homebuilding has shown scattered signs of improvement. One broker reported a recent increase in sales of lots for lower-priced homes to developers. Contacts, however, said that multifamily construction remains at minimal levels with little improvement expected in the near future.

Commercial construction remains depressed with high office and retail vacancy rates in many District cities. Contacts do not expect much new construction activity for the next several years. Several blamed lack of financing for curtailed commercial construction.

Wages and Prices: Contacts report ample supply of qualified workers with wage and input prices remaining relatively stable. Transportation firms are posting flat to slightly higher shipping rates. Citrus prices are holding up in a strong market.

SEVENTH DISTRICT--CHICAGO

Summary. Most sectors of the District economy softened over the past six weeks, although there were signs of improvement in several key sectors. Reports from retailing contacts suggest that sales over the holiday season were essentially flat with a recessionary year-earlier period. Auto sales generally remained weak around the District, although several large dealers reported solid sales improvement in recent weeks. Combined car and light truck production schedules call for first quarter 1992 assemblies to be even with the fourth quarter of 1991 on a seasonally adjusted basis. New softening in production outside the auto industry also contributed to recent weakness in District manufacturing activity. As a result, District manufacturing employment softened as the year ended. Lower home mortgage interest rates have mainly generated higher levels of refinancing activity, but have also sparked some improvement in the District's home resale market.

Retail Sales. District retail sales for the holiday season were about flat with weak sales last year, despite widespread discounting and heavy promotional activity. Large retailers reported that sales in the District generally followed the national pattern. This is in marked contrast with last Christmas, when District sales held up well compared to the national average. One large chain stated that discount-driven sales gains (on a year-over-year basis) recorded in the last two weeks of December reversed a sharp year-over-year sales decline early in the holiday season. Sales strength was concentrated in soft goods, and inventories of many items, especially "big-ticket" appliances, remained above plan. Another large chain reported that year-over-year sales gains improved as December progressed, with small appliances performing relatively well. This chain's sales in District markets were mixed, but showed some improvement from previous months on a seasonally adjusted basis. The company's inventory remains well above plan, and the firm is committed to cutting stocks further. A large survey of independent retailers in Illinois and Northern Indiana indicated that year-over-year sales declines worsened over the latter half of 1991. The preliminary results of a post-holiday survey of Michigan retailers showed that the percentage of stores reporting year-over-year sales declines for the holiday season was well above "normal" levels. A manufacturer's representative stated that financing receivables from several large discount chains grew increasingly difficult in recent months, citing growing lender concern with the retailers' credit quality.

Autos. Reports from auto industry contacts generally indicated continued weakness in both car sales and production, although two recent reports from large auto dealers suggested some improvement in consumer demand. A supplier of financial services to many District auto dealers reported that most dealerships' sales remained weak. A domestic auto producer stated that dealer orders remained weak, and

showroom traffic has yet to improve from fourth quarter rates. Reports of continued sluggishness in auto sales are not universal, however. One of the largest dealers in the District stated that sales improved markedly during December and early January, citing improvement in customer and salesperson confidence. This dealer has begun to rebuild inventory, after remaining extremely cautious over the latter half of 1991. Another large dealership is optimistic about sales in the first half of 1992, and recently ordered a "slew" of lower-priced new cars in anticipation of a surge in sales. Declining interest rates have substantially reduced this dealership's inventory financing costs. An auto industry analyst expects combined car and light truck production in the first quarter of 1992 to be essentially flat from the fourth quarter of 1991 on a seasonally adjusted basis, although first quarter car production depends on planned assemblies that have been pushed forward into March. If sales do not improve as the first quarter progresses, this analyst expects production schedules to be cut further, making the auto sector a drag on the District economy.

Manufacturing. Purchasing managers' surveys and direct contacts suggest that the recovery in District manufacturing activity stalled late last year, and industrial production in the District may have declined on a seasonally adjusted basis. The Chicago purchasing managers' survey index, like that for the nation, weakened in December, and dropped below 50 percent for the first time since June 1991. Significant declines in the production, new orders, and order backlogs components accounted for most of the weakness in the overall Chicago index, while the inventory and employment components remained below 50 percent. Likewise, the most recent surveys in Detroit, Milwaukee, and Southwest Michigan each indicated some loss of momentum. A large appliance manufacturer stated that first quarter shipments were expected to be below a weak year-ago period. A large manufacturer of heavy equipment noted that orders from customers in primary metals, paper, and petrochemical industries remained soft in December and early January, with little sign of a turnaround in sight. A large manufacturer of communications equipment reported that orders remained mixed, citing weak demand from two key markets -- construction and state and local governments. At the same time, this manufacturer stated that December orders for semiconductors were the highest for that month since 1987, despite continued weakness in orders from the auto and personal computer markets.

Employment. In November, total payroll employment in the District fell significantly on a seasonally adjusted basis, led by the first drop in District manufacturing employment since April. The continued decline in national manufacturing employment in December was concentrated in several key District industries, including industrial machinery and fabricated metals. The results of purchasing managers' surveys also suggest that District manufacturing employment continued to weaken in

December. The pace of layoff announcements by District firms appears to have increased in recent weeks, and could affect future employment in a wide variety of industries, including consumer goods manufacturing, transportation, technology, and communications. Most of the major plant closings that are likely to follow General Motor's restructuring announcement are expected to be outside of the District, but the impact on white-collar employment and independent parts suppliers will put a further drag on District employment. Unemployment rates in Illinois, Indiana, and Michigan have been running above the national average, and Illinois' unemployment rate rose from 7.7 percent October to 9.3 percent in December. The District employment outlook still has some bright spots, however. Several Chicago-area executive recruiters reported significant increases in recent weeks in the number of manufacturing firms looking to hire people, although improved demand has been concentrated in requests for higher-skilled personnel. A placement firm specializing in technically-oriented sales and marketing personnel reported that "business is booming." After a significant decline in the first three quarters of 1991, this firm enjoyed a record fourth quarter. Another placement firm noted that "we are seeing a lot of optimism on the industrial side." One recruiter stated that strength in demand was even evident in the steel industry.

Real Estate/Construction. Reports from District realtors and financial institutions indicate that lower home mortgage rates have principally affected refinancing activity, but have also helped spark some improvement in the existing-home sales market. A large realtor reported the best December sales month in its history, with transaction volume substantially higher than in December 1990. One financial analyst stated that consumers' gains from refinancing could be postponed, however, as refinancing volume is taxing processing capacity. This contact reported that smaller banks appeared to be increasingly interested in making new residential mortgage loans in recent weeks. Commercial construction remains weak, and cement shipments and construction contract awards suggest that overall building activity in the District is now about as weak as it is nationally. A large cement producer specializing in commercial construction in the Chicago area reported that shipments declined substantially in December from the previous year, and the December decline was much sharper than the decline for the year to date. The outlook for this firm's cement shipments is supported by the prospect of higher public works spending in 1992, and the firm is also seeing improvement in demand for cement used in residential construction projects. Not one respondent to a recent nationwide survey of commercial real estate professionals expected property prices, on average, to rise, from 1991 to 1992. The anticipated median price decline in the Chicago area was larger than decline expected for the nation as a whole.

EIGHTH DISTRICT - ST. LOUIS

Summary

Manufacturing activity remains weak in the District, but some firms report increased activity. The health services sector continues to add employees. Retailers report holiday sales comparable to year-ago levels. Residential construction continues to improve, although construction financing is still a constraint for some builders. Loan demand remains depressed, especially in the consumer loan categories. District farmers report low cotton and hog prices, but strong wheat prices.

Manufacturing

Although District activity remains slow in the manufacturing sector, several bright spots were noted. For example, an electrical equipment contact reports that orders were steady last month and inventories were in good shape relative to demand. A power tool manufacturer in Arkansas reports strong sales, especially in its export markets. A paper manufacturer reports stable sales for its packaging paper, but declining sales of paper for advertising supplements. A paper products company announced the development of a new plant with about 200 employees in Bowling Green, Kentucky.

Employment

The District has been spared the brunt of recent cutbacks in the domestic auto sector because the models produced in the region are strong sellers. In fact, one Missouri auto plant has recalled at least 1,000 workers for a third shift because of continued strong demand for

minivans. Two months after laying off 1,300 employees, the nation's largest shoe manufacturer announced another round of plant closures, affecting 1,150 workers throughout Missouri. Reasons stated for the closures include high labor costs and a "truly terrible" market for shoes. A Kentucky tire manufacturer recalled its workers to replenish its inventory, reflecting a new contract with a domestic auto maker. Growth in service-sector employment has cushioned some of the losses in goods-producing sectors. For example, a telecommunications firm in Memphis plans to add 100 workers, the second increase in six months. In St. Louis, growth in health services jobs (2,800 in 1991) has helped offset cutbacks at the area's major firms.

Consumer Spending

Retail sales in the District were mixed for the 1991 holiday season. St. Louis and Memphis contacts report sales of non-auto merchandise were little changed from last year, while the Louisville and Little Rock regions posted modest to significant increases. Apparel, electronics, jewelry and small-ticket items sold well, as contacts believed consumers were looking for values. Big-ticket items were more heavily discounted than general merchandise; however, price-cutting overall was at the same level as last year. Inventories in St. Louis and Memphis are currently at desired levels, while reports from Little Rock and Louisville state that inventory levels are lower than anticipated because of careful buying by store managers and a favorable holiday shopping season. Despite cautious optimism about the first quarter, many retailers do not expect sales to pick up until later in the year.

Construction and Real Estate

District homebuilders report flat or modest activity in new home construction. The exception is in northwest Arkansas, which

continues to show strong growth in both single- and multi-family home construction. Most District builders believe the industry has bottomed out and that conditions will improve significantly by mid-1992. Construction financing is still reported to be constrained. Despite the lowest mortgage rates since the mid-1970s, many buyers are still hesitant to commit because of job security concerns. New and existing home prices are relatively stable, despite increases in materials costs for builders. The nonresidential construction sector, with the exception of public works projects, is still very weak throughout the District.

Banking

Loans on the books of District banks are still flat or declining. The lackluster holiday sales season is reflected in consumer lending data: consumer loans declined 1.6 percent at the District's largest banks during the last four months of 1991. The only major category of loans to show growth during the last third of 1991 was commercial loans, which rose 0.3 percent. District bankers report that most real estate loan activity is related to mortgage refinancing.

Agriculture and Natural Resources

The winter wheat crop in the District is in mostly fair to good condition, except in parts of Arkansas where flooding has caused some damage. Wheat prices remain relatively strong. Contacts report weak or falling prices for cotton and hogs, while cattle prices have firmed. Livestock is mostly in good condition. Lumber producers in the District report weak demand; however, Southern Pine lumber producers report that prices held firm through the end of the year. Coal production, although down by 8 percent from last year, has increased significantly in recent weeks.

NINTH DISTRICT—MINNEAPOLIS

The District's economy has been largely stagnant lately. Labor market conditions generally deteriorated. Retail sales increases were modest, except in those areas that continue to benefit from the influx of Canadian shoppers. New auto sales remain weak, though truck sales have rebounded sharply. Construction and manufacturing conditions were mixed. Agriculture did well, with high crop yields offsetting price declines. Tourism has remained strong.

Employment, Wages, and Prices

The November unemployment rate in Minnesota was 5.0 percent, slightly higher than its 4.7 percent rate of the month before, but substantially above its year-ago level of 3.9 percent. The growth of Minnesota's nonagricultural employment in November was only 0.38 percent over the last year, with declines in all sectors except government (up 1.02), transportation (up 0.27), and finance, insurance, and real estate (up 1.36). In particular, manufacturing (down 1.47), mining (down 1.18), and construction (down 7.68) all posted substantial declines. The November unemployment rate in Montana, at 7.4 percent, was also higher than it was a month ago (6.2) or a year ago (6.8). This weakness was also reflected in the anemic growth of Montana's nonagricultural employment in November, up only 0.96 percent from a year ago. The November unemployment rate at 4.0 percent was higher than its month-ago (3.4) or year-ago (3.3) levels in North Dakota. November's unemployment rate was higher in the Upper Peninsula (up to 11.7 percent from 9.8 percent a year ago) and western Wisconsin. The only part of the District in which the unemployment rate fell in November was South Dakota, which at 2.8 percent was down only 0.1 percent from the previous month and 0.4 percent from a year ago. South Dakota's economic strength was also reflected in nonagricultural employment growth which was up 3.0 percent in November relative to a year ago.

Consumer Spending

Holiday retail sales in the District showed very modest growth. A number of major retailers reported sales increases in comparable stores ranging from 1 to 6.5 percent in December relative to a year ago, with discount chains reporting increases of 6 to 16 percent over the same period. Retailers also reported more frequent bad checks and shoplifting. Retail sales continued to be strong in those parts of Montana, North and South Dakota, and the Upper Peninsula of Michigan within a reasonable drive from the border due to the continuing influx of Canadian shoppers, and hotel occupancy rates in these areas were quite high.

New truck sales surged in December with some dealers reporting sales increases of 83 percent in December relative to a year ago. However, year-to-date truck sales were still 9 to 13 percent below last year's level. New car sales in the District improved in December, but continue to be weak, with local dealers of domestic cars reporting year-to-date sales declines ranging from 20 to 25 percent, while foreign car dealers reported flat year-to-date sales in October. Used car sales continue to be strong.

Housing sales improved in the District. In the Minneapolis--St. Paul area, housing sales were up 13 percent in the fourth quarter, and 3.8 percent year-to-date. This was despite the fact that sales fell slightly in December relative to the previous month, and were essentially unchanged from their year-ago level.

Tourist activity has been excellent in the District. Yellowstone National Park had its best year ever. Total bridge crossings onto the Upper Peninsula of Michigan this year have been above their year-ago levels, with crossings over the Mackinac and International bridges in November and December up 4.8 percent and down 0.3 percent, respectively, relative to their year-ago levels. The upcoming Super Bowl is expected to bring \$45-\$50 million in direct expenditures to the Minneapolis-

St. Paul area. Heavy early snow fall got the skiing and snowmobiling seasons off to a good start, but the lack of recent snow has slowed winter recreation considerably.

Construction and Manufacturing

Conditions in the District's construction industry have been mixed. The November level of new housing permits in Minnesota was down 5.6 percent relative to a year ago, while commercial construction in the Minneapolis-St. Paul area continues to be depressed. Elsewhere, construction is reported to be doing well in North and South Dakota, and holding its own in Montana.

Conditions were mixed in the District's manufacturing industries. In Minnesota, average weekly hours at 40.8 in November were slightly higher than their year and month-ago level of 40.5. In contrast, Minnesota's November average hourly earnings were up only 2.8 percent relative to a year ago.

Resource-Related Industries

High crop yields in the District generally more than offset price declines in 1991. Dry beans and potato production are at record levels in both North Dakota and Minnesota. Top soil moisture is in good condition for spring planting. Recent milder weather has stirred some concern about spoilage in the sugar beet crop. Minnesota's mid-December all farm products crop price index was down 1.5 percent relative to its year ago level, with crop prices up 1.0 percent, livestock prices down 17.0 percent, dairy products up 21.6 percent, and poultry products down 2.7 percent over this period. Uncertainty about future farm income has depressed farm machinery sales somewhat.

Mining conditions have been mixed in the District. Copper prices are holding firm, but oil and molybdenum prices remain low. The lumber and wood products market is mixed, with problems due to environmental issues anticipated in the near future.

TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy still appears to be growing slowly but unevenly. Retail sales are up modestly, with Christmas sales apparently somewhat better than a year ago. Housing activity also continues to improve. But signals from the manufacturing sector are mixed, auto sales are down, and energy activity is slackening. Moreover, the farm sector has retreated somewhat from its recent peak performances. Prices generally remain steady both at retail and for many manufacturers' inputs. Most retailers are satisfied with current inventory levels, while manufacturers are striving to reduce their inventories of materials and other inputs.

Retail Sales. Retail sales have improved slightly over the past month, with apparel sales accounting for much of the improvement. Sales were generally weak, however, with Christmas sales up only modestly from last year. Just a slight improvement in sales is anticipated this year. Retailers report stable prices over the past month and expect small price increases in 1992. Most retailers are satisfied with current inventory levels and expect little change in the coming months.

Auto sales declined slightly in the district over the last month. Some potential buyers still find it difficult to get loans due to tighter credit standards. While automobile dealers expect sales to begin picking up in the next few months, most of them are still trimming inventories.

Manufacturing. Purchasing agents report mixed price changes. The prices of metals and fuel have fallen, while the prices of some manufactured components have increased. Agents expect prices to remain stable for the next few months. Materials are readily available. Most firms have been trimming inventories and plan further reductions. Plants are generally operating below

capacity. Exports have risen in recent months, especially for firms with markets in Mexico and South America.

Energy. Energy activity in the district has weakened recently due mainly to falling oil prices and an outlook for soft prices throughout the year ahead. The average number of operating drilling rigs in district states decreased from 237 in November to 228 in December. The December rig count was 33 percent below its year-ago levels.

Housing Activity and Finance. Housing starts in most areas of the district increased somewhat from the previous month and were much higher than a year ago. Builders expect starts to increase further in the first quarter of 1992 and in the year as a whole. The prices of some building materials, especially lumber, have increased. Sales of new homes are higher than a year ago, with prices higher in some district areas but unchanged in others. According to most survey participants, inventories of new homes are below normal.

Most district thrift institutions report deposit outflows during recent months. Respondents expect outflows to continue at a steady pace over coming months because of low rates on deposits. Mortgage rates have dropped at least 100 basis points over the past three months but are expected to level off in coming months. Mortgage demand and commitments are strong due largely to refinancing. Respondents expect mortgage demand to remain strong during coming months, due to both refinancing and new home purchases.

Banking. Changes in total loan demand were mixed last month, with half of the respondents reporting no change and equal numbers of the remaining respondents reporting increases and decreases. Demand for home mortgages rose, while demand for consumer loans, construction loans, and commercial real

estate loans were flat to down. Loan-to-deposit ratios were generally unchanged from the previous month but lower than a year ago.

All respondents reduced their prime rates last month and almost all expect to leave these rates unchanged in the near future. More than half of the respondents also reduced their consumer lending rates last month, and a few expect to lower rates further in the near future. Lending standards were unchanged.

Deposits increased at most reporting banks. Increases in demand deposits, NOW accounts, and MMDAs outweighed decreases in large CDs and small time deposits.

Agriculture. After a poor start, the winter wheat crop has improved due to recent widespread precipitation. The crop's condition is now average to above average in most areas. More moisture is needed to ensure further crop development due to dry subsoil conditions in parts of the district.

Yearend credit reviews for district farm borrowers showed little change from a year ago in the number of problem loans. But credit reviews did reveal a growing disparity between livestock and crop borrowers. Bankers report that some livestock producers struggled to repay loans as cattle and hog prices slumped in the last half of 1991, while crop farmers benefited from rising wheat prices. Bankers expect the divergence in crop and livestock incomes to continue in 1992. Nevertheless, bankers expect only a slight increase in problem loans overall.

Bankers expect farm loan demand to be steady in 1992. Demand for livestock loans may fall, while demand for wheat operating loans may edge up as farmers take advantage of higher wheat prices. A few banks report increased demand for real estate loans as nonfarm investors move funds out of certificates of deposits to purchase farmland.

ELEVENTH DISTRICT--DALLAS

Economic activity has been flat or slightly down. Heavy competition has reduced selling prices and profits in several sectors. Manufacturing activity has been stagnant and may be declining. Retail sales improved in December. Overall Christmas sales were equal to or slightly higher than last year's level. Retail respondents report higher than desired inventories. Many respondents conclude that consumers are concerned about the economy because of announced and anticipated layoffs. Most respondents do not expect activity to increase until the second quarter of 1992 or later.

Retail sales improved in December. Overall Christmas sales were equal to or slightly above last year's level. Retailers report much stronger sales at discount stores than at non discount stores. Most respondents note higher than desired inventories, particularly in apparel. Selling prices have been very competitive, and some respondents have reduced profits to decrease inventory. Automotive sales remain slow.

District manufacturing activity has been stagnant and may be declining. Apparel production has slowed but remains above last year's level. Chemical production has been flat, with some weakness in the demand for plastics. Chemical producers are concerned about overcapacity and do not expect orders to rise until the third quarter of 1992. Domestic demand for oil field machinery has been stagnant despite an expected seasonal increase. Prices have fallen. Growth of international demand has slowed but remains positive. Prices have also fallen as demand declined for petroleum refining and electrical and electronic machinery. Overcapacity in the supply of primary metals has reduced prices and cut profits in that sector. Demand for

fabricated metals is well below last year's level. One exception is the producers serving the petrochemical industry, who experienced a pick-up in demand for equipment that helps meet the standards of the Clean Air Act. Production of paper products remains slow but above last year's level. Some paper producers report higher than desired inventories. Environmental concerns continue to restrict the supply and boost prices for lumber and wood products. Producers are optimistic that lower interest rates will increase demand soon. Recent wet weather has helped depress the demand for cement, except along the Texas-Mexico border, where demand remains strong. Cement producers express optimism about the prospects for a substantial increase in demand--primarily from an increase in federal funding for highways.

District construction activity is up slightly but shows signs of a slowdown. Construction of single-family housing has increased modestly, but a drop in housing permits probably indicates that growth may be negative. Although respondents report tight credit conditions are moderating growth, apartment activity has been strong. Industrial and office real estate demand is flat. Non-building construction has increased moderately, and respondents expect an increase in federal funding will boost highway construction.

Demand for District services has not increased and may have softened slightly. Heavy competition has decreased selling prices, except for airfares, where bankruptcies in the industry have reduced competition. Some service respondents noted rising costs and reduced profits. Accounting services report an increase in demand for bankruptcy and corporate financial services.

Low oil and gas prices are creating a somber 1992 outlook for the energy sector. High OPEC production and expectations of Iraq and Kuwait's reentry into the oil market have lowered oil prices. After hovering around a \$20-per-barrel average in 1990, the price of oil dropped to \$17.50 in mid-January. Natural gas prices reached 14-year lows during the summer, and warm weather in the fourth quarter has not spurred much of a price increase. The average wellhead price of natural gas in 1991 was 15 percent below that of 1990. Current low prices and prospects of further declines in the second quarter have reduced exploration and production activity in the nation and the District. Some oil and gas producers are shifting their exploration activities overseas. Many energy and related companies have announced layoffs.

District commercial loan demand is reported to be steady or declining slightly. Banks report excess liquidity and indicate that they are having trouble finding quality credits. Activity has increased for refinancings and first mortgages.

Severe weather has damaged agricultural production and reduced farm and livestock income projections. Livestock prices are below last year's level. Crop prices are mixed with higher prices for corn, grain sorghum and wheat but lower prices for cotton, cottonseed, hay, peanuts and soybeans.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic weakness persists in much of the Twelfth District, although intermountain regions remain relatively healthy. Christmas sales were generally below expectations, although some pickup in post-holiday sales was reported. Manufacturing continues to contract in California, and little growth is reported in other parts of the District. Real estate markets are generally sluggish, but residential sales activity shows some signs of bottoming out. Wage and price increases are modest, with the exception of health care. Significant mortgage refinancing activity is reported by lending institutions, though other loan demand remains weak. Consumers are reported to be using the savings from refinancing to reduce other debt levels, or shifting to shorter-term mortgages to build equity more quickly. Agricultural and resource industry conditions are mixed, with livestock and timber sectors reporting stress.

Business Sentiment

Economic expectations of Twelfth District business leaders remain subdued. Thirty-one percent of respondents now expect output to decline in at least two of the next four quarters, compared to 25 percent in November and 7 percent in September. An additional 56 percent expect the economy to expand, but at a rate below 2.5 percent. At the same time, the proportion of business leaders expecting improved business investment, consumer spending, and housing starts increased from November. The most optimistic expectations of business leaders were for housing starts, where 58 percent of the respondents projected some improvement in the next four quarters. Eighty-seven percent expect inflation to decline or remain stable.

Wages and Prices

Upward pressures on wages and prices remain minimal throughout most of the Twelfth

District. Retailers are reported to have engaged in heavy discounting in response to sluggish holiday sales. Wage and price cuts also are reported in service sectors, including consulting, money management, entertainment, catering, and teaching. A significant exception is health care, where health benefit plan prices are expected to rise 8 to 20 percent in 1992. Lumber prices have been flat since mid-July, and most commodity prices are flat or falling. Most wage increases in the Twelfth District are reported in the 3 to 4 percent range, although manufacturing wages in Washington are reported to be rising 4 to 6 percent.

Retail Trade and Services

Christmas retail sales in the Twelfth District were generally at or below their weak 1990 levels, even with aggressive discounting used to attract wary consumers. Sales in California were down somewhat from last year. Low-end retailers appear to have had a slightly better experience. Sales in Utah and eastern Washington were strong. One retailer reports that in the eight days since Christmas, sales in California have been encouraging, about 5 percent above expectations.

Auto sales are reported flat in California and down in the Puget Sound area, but show improvement in Idaho. Firms doing business with state and local governments are cautious due to budget problems, and are hiring consultants on contract rather than increasing the number of full-time employees. The demand for legal services is flat. The health services sector, however, continues to add jobs.

Manufacturing

Manufacturing activity in the Twelfth District remains sluggish, with the number of jobs in California continuing to contract due to cutbacks in aerospace and electronics. Boeing, however, is still producing at full capacity and new orders for commercial aircraft, which had fallen in 1991, picked up in mid-December. The capital spending plans of several respondents remain little changed, apparently unaffected by recent interest rate cuts, though a major upgrade of an

aluminum smelter was recently announced in eastern Washington.

Agriculture and Resource-Related Industries

Agricultural conditions in the Twelfth District are varied. Cotton, cattle, and fruit prices are down. Excess supply and falling consumer and export demand for beef has caused significant losses among feedlot operators. Losses are also reported by Idaho bean and potato growers due to low prices. Oregon agriculture, however, has had its best year in 10 years. Court injunctions have nearly halted federal timber sales in Washington and Oregon. Lumber product markets face moderate demand and price increases are expected.

Construction and Real Estate

Construction and real estate activity remains slow in much of the Twelfth District, with no significant effect yet seen from recent interest rate declines. In California, the housing industry is stagnant with prices of some upper-end homes dropping a reported 10 to 15 percent from their previous peak. The number of sales of existing homes, however, edged up in December after declining since May. Conditions are reported weak in Washington, with some slippage in home prices. Contacts in Arizona, however, report a slight increase in housing starts. Farm and ranch real estate sales in Idaho are off 50 percent from a year earlier due to weak agricultural conditions.

Financial Institutions

Twelfth District financial institutions report a significant increase in mortgage refinancings due to recent interest rate declines. The resulting savings, however, appear to be used for debt reduction rather than consumer spending. One-third to one-half of refinancing applicants are reported moving to a 15-year mortgage to build up equity with little change in payments. Outside of refinancings, loan demand remains sluggish, and margins are being compressed by lower interest rates. Weak earnings continue due to problem real estate loans.