SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS

BY FEDERAL RESERVE DISTRICT

JANUARY 1993
TABLE OF CONTENTS

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

Reports from the twelve Federal Reserve districts indicate continued improvement in economic conditions across much of the nation. Conditions are mixed, however, in the San Francisco district where weakness in California continues to offset moderate growth in other district states. Retail sales during the holiday season were significantly better than a year earlier in most districts, generally fulfilling or exceeding retailers' expectations. Manufacturing activity is steady to increasing moderately in nearly all districts, but this improvement may not be reflected proportionately in labor markets. District reports contain little evidence of significant upward pressure on prices. While the residential sector continues to improve in most districts, commercial real estate markets generally remain weak. Overall loan demand at financial institutions is rising slightly in most districts. In agriculture, record yields of fall crops have pushed prices down, but gains in the livestock sector are expected to help boost overall farm income slightly.

Retail

Sales in the holiday season posted significant year-over-year gains in most districts, with mixed results in the San Francisco district and in the Northeast. Sales gains were smaller in California than in other states in the San Francisco district, and a minority of retailers in the Boston district reported flat sales. Retailers in several districts reported sales better than expected. In a number of districts, merchants noted that sales gains

* Prepared at the Federal Reserve Bank of Kansas City based on information gathered before January 12, 1993. 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.
were achieved without the heavy promotions and aggressive price cutting of recent years.

A wide range of merchandise apparently sold well, with some regional variation. In the St. Louis district, sales mainstays included jewelry and smaller appliances and electronics items. Atlanta reports significant increases in sales of goods ranging from apparel to big-ticket durables. In the New York district furniture and rugs sold well. Merchants in the Chicago district noted that sales held up well in the post-holiday period, especially sales of big ticket durables, including major electronics, appliances, and furniture. Retailers in the Richmond, Atlanta, St. Louis, and Kansas City districts expressed optimism for further sales growth in early 1993.

Manufacturing

Manufacturing activity is reported to be steady to increasing moderately in nearly all districts. Activity appears to be flat to expanding modestly in the Boston, Philadelphia, and Richmond districts. Stronger but less than robust activity is reported by Cleveland, Atlanta, Chicago, St. Louis, and Dallas. San Francisco reports that Twelfth District manufacturing activity continues to contract, due to further weakening in aerospace and defense-related industries in southern California and Washington; manufacturing shows some improvement, however, elsewhere in the district.

Manufacturing activity in the Cleveland and Chicago districts has been boosted by increased motor vehicle production and related increases in the output of steel and tires. As a result, Cleveland reports rising capacity use ratios for some steel producers, while strong demand has pushed production close to capacity for some tire producers. Boston, Atlanta, and Dallas report some increases in the production of housing-related products, such as
furniture and construction materials. Capital goods producers reported an uneven but rising trend in their business, with uncertainty about a possible investment tax credit leading to some postponements of orders.

The moderate improvement in manufacturing activity may not be reflected proportionately in labor markets. Boston reports that half of its respondents expect their work forces to remain at the current level, while the remaining respondents expect to implement reductions. Most of the manufacturers contacted in the Philadelphia district were holding employment steady. In the Cleveland district, most manufacturers believe they can increase production with their existing work forces. Some firms in the St. Louis district expect to add jobs, however, and a major home appliance manufacturer has recalled a large number of laid-off workers and expects to add substantial new hires. In the Minneapolis district, layoffs by two computer equipment firms and an airline have been partly offset by new hiring elsewhere in the district.

Construction and Real Estate

The residential sector continues to improve in most districts. Home sales, as well as housing starts and permits, were generally better in 1992 than in 1991. Lower mortgage rates, increased consumer confidence, and pent-up demand were cited as responsible for the improvement. Boston reports slow but steady improvement in its residential real estate market. While Kansas City notes a recent slowing in housing activity, Minneapolis reports its busiest winter construction season in six years. Some glimmers of hope for multifamily construction also appear, as both Atlanta and Dallas report rising occupancy rates and firming rents. San Francisco reports mixed conditions in its residential sector. House prices have weakened further in southern
California and softened in parts of Washington, but have risen in Oregon and Utah.

Commercial real estate markets remain generally weak, but there are some positive signs here and there. The office vacancy rate in downtown Buffalo, while still high, fell in 1992 for the first time in four years. Activity in the Richmond district's nonresidential sector has increased in recent months, with vacancy rates falling in some areas and more inquiries from businesses in strong financial condition. Nonresidential construction has been expanding in the St. Louis area, primarily in public works and new factories. Minneapolis also reports a sharp rise in public works contracts, as well as in construction of some new shopping malls across the district. One of the new malls was built in a border town to cater to strong demand by Canadian shoppers. Nonresidential real estate markets remain weak in much of the Dallas and San Francisco districts. Vacancy rates are still high in Dallas, but prices there have fallen enough to bring a pick-up in property sales. Several markets are weak in the San Francisco district, where commercial rents and property values are depressed by high vacancy rates and continued employment losses.

Financial Services

Financial institutions report a further slight increase in overall loan demand in most districts. Philadelphia, Cleveland, Richmond, Atlanta, St. Louis, and Kansas City report slow growth in business loans. New York reports slow growth in business loans by small and midsized banks. Most districts note a drop-off in mortgage lending, reflecting reduced demand for refinancing. Dallas reports little change in loan demand, and San Francisco notes mixed conditions in the Twelfth District. In California, loan demand is
weak and the volume of outstanding loans continues to fall. Some growth in loan demand is evident, however, in Arizona, Utah, and Washington.

**Agriculture and Resource-Related Industries**

Despite some unseasonably wet weather in parts of the Richmond, St. Louis, and Kansas City districts, fall crop yields have been near record levels. Large supplies of corn and soybeans have pushed prices down, thus restricting income gains for crop producers. But lower crop prices also mean lower feed prices and likely income gains for livestock producers. Overall, farm income is expected to be up slightly in 1993 and farm operators are seen as likely to maintain their solid financial condition.

Metal mining continues to be weak in the Minneapolis district, where slack orders have led to two iron mine shutdowns and substantial layoffs. Dallas reports a slowing in energy industry activity, although Kansas City cites a recent rise in the number of operating drilling rigs in its district. Both districts agree that drilling is likely to drop sharply in the near term, however, because certain tax incentives for drilling expired at the end of 1992. Dallas also notes that low margins have led many refiners to reduce their capacity.

Conditions in the lumber and wood products industry vary somewhat across the nation. St. Louis notes that orders at southern pine lumber mills are down slightly, although production remains well above last year's level. San Francisco reports that orders for wood products are firm and inventories are low, while Minneapolis reports strong demand for lumber and for plywood substitutes.
Economic activity in the First District was increasing very modestly at the end of 1992. Retailers reported mixed holiday results: while sales improved for a majority of contacts, a minority experienced flat results. Most manufacturers report that sales were level or only slightly above year-ago levels. Sales volumes were up for residential real estate and insurance. Although the majority of contacts expect a modest business upturn in 1993, they do not intend to hire and may even reduce their work forces.

Retail

Although media reports indicated a robust Christmas season, not all First District retailers experienced improvements over year-ago results. Sales gains ranged from substantial to none. Some of the variation is geographic; the strongest sales advances were made by retailers serving national markets. Further, several retailers who reported no increase in sales attributed their weak performance to store locations in New England but outside the Boston metropolitan area.

Some contacts promoted heavily or resorted to markdowns, and margins varied approximately in line with these activities. Inventories are now even with or slightly above last year's levels; only one contact believes that inadequate stocks reduced holiday sales.

Some firms experiencing sales gains added permanent employees or granted wage increases. Similarly, capital expenditure programs parallel recent sales activity. These plans range from equipment upgrades to major expansions. Most retail contacts do not expect dramatic changes in the economy or their own performance in 1993.
Manufacturing

About one-half of this month's manufacturing contacts report that recent sales are flat relative to year-earlier levels. Most of the remaining companies indicate that their overall business has improved modestly. Many consumer and housing-related products and business services have experienced an increase in demand. Automobile markets remain mixed. The press has reported that a New England-based military contractor has received a large order from Saudi Arabia, but our contacts indicate that other defense business is weakening. Orders for aircraft parts, large electronics systems, and government work also are softening. Japanese and European markets have been weak for several manufacturers.

Respondents report that they face a highly competitive pricing environment. Business customers in the retail, aircraft, and automotive industries in particular are pressuring suppliers to reduce prices.

The majority of the manufacturers polled expect that continued growth in the U.S. economy will have a positive, though relatively modest, impact on their companies in 1993. Most manufacturing contacts have reduced employment in the past year, with declines ranging from 1 to 25 percent. Only one, relatively small, manufacturer indicated that a significant increase in production jobs is likely this year. Roughly half the sample expect that their U.S. work forces will remain at about the current level, while the remaining firms intend to continue to implement reductions.

Capital spending trends and plans are mixed. Many contacts indicate that they are investing in new computers. Although most manufacturers contacted have pared down inventories over the past year,
some believe that they can make further progress by adopting better inventory control methods.

**Residential Real Estate**

The market for residential real estate in the First District is continuing to show signs of slow, steady improvement. Sales volume is above year-ago levels, inventories are down slightly, and permits are up a bit. A New Hampshire contact reported November sales that were at 1987 levels. A Connecticut contact was less optimistic about reported sales increases, noting that many may be due to foreclosures and distress sales rather than marketplace improvements. Single-family home prices seem to be flat, while condominium prices may still be falling.

**Nonbank Financial Services**

Insurance companies have experienced a modest increase in sales in the last several weeks. However, most report sales flat over the year, with only a few citing increases compared to year-end 1991. Mutual funds, variable annuities, and individual life insurance products continue to be strong sellers. Respondents continued to retreat from personal property-casualty lines, especially for automobiles and for properties in the Northeast. Most contacts have either reduced employment in the last quarter or foresee a reduction in 1993. Only one plans a small increase in employment this year. Assets under management have shown mixed trends, but most firms have strengthened their capital positions for the year.
On balance, economic developments seemed slightly more positive in recent weeks, although some negative reports continued to be received. Most District retailers had sales results that were either on or better than plan in November and December. Solid gains were posted for apparel of all types, and year-end inventories were described as generally in good shape. Unemployment rates in New York and New Jersey continued their seesaw pattern but are somewhat lower than their October levels. Office leasing activity proceeded at a fairly good pace in midtown Manhattan but remained sluggish in downtown Manhattan. Meanwhile, downtown Buffalo recorded the first decline in its office vacancy rate in four years, and a larger percentage of Buffalo purchasing managers reported higher new orders and/or production. Homebuilding activity was relatively slow, but new home sales were generally above year-earlier levels. Most senior loan officers at small and midsized banks indicated no change in their willingness to lend.

**Consumer Spending**

Most District retail contacts reported sales results that were in line with or better than projections in November and December. A severe storm closed District stores for one or two days in mid-December due to hurricane-force winds, widespread flooding and heavy snows, but apparently sales were recouped, at least in part, during the remainder of the month. While the sales environment has remained highly competitive, retailers stated that they engaged in less promotional activity and price-cutting than during the 1991 holiday season with somewhat higher profit margins as a result. Most contacts noted more enthusiasm and a less conservative attitude on the part of consumers, but our contacts were reluctant to assert that a turning point has been reached. Over-the-year sales changes ranged from -9 percent to +8.5 percent in November and from flat to +12.5 percent in December. The Retail Council of New York State’s annual survey of about 200 stores found sales gains averaging 6 to 8 percent above the 1991 level for the post-Thanksgiving through post-Christmas period.
A wide variety of merchandise sold well during November and December though reportedly the best sellers were practical items such as cold weather gear (especially after the December storm), furniture, rugs, and accessories. Children's books, video games and remote control toys were also popular.

**Residential Construction and Real Estate**

Homebuilding activity has been relatively slow in most of the District due both to the season and to the unwillingness of potential buyers in some areas to commit themselves given their continuing uncertainty about jobs and the economy. For 1992 as a whole, new home sales were generally above the sluggish, year-earlier levels with the gains varying widely within the District. Most builders anticipate some further improvement in 1993. Renewed sales activity was reported at previously stalled projects in Westchester County and central New Jersey. Developers intend to expand these projects if buyer interest continues. Restoration and rebuilding of homes that were damaged or destroyed in a severe December storm will provide a further impetus to building activity, especially in flood-ravaged coastal areas.

Office leasing activity continued at a fairly good pace in midtown Manhattan, but has remained sluggish downtown. Vacancy rates moved up in both parts of Manhattan. Net absorption of space remained negative as a result of the completion of a new office building in midtown and the continuing additions of existing space in the downtown market due to corporate restructurings. An annual survey of office space in downtown Buffalo found an almost three percentage point decline in the vacancy rate between year-end 1991 and 1992. Although the rate remains high, this was the first decrease in four years.

**Other Business Activity**

District unemployment rates continued their seesaw pattern since the last report, but on balance declined somewhat. In December, New Jersey's unemployment rate was 8.0 percent, down from 8.7 percent in November, but New York's was 8.4 percent, up from 8.0 percent one month earlier. However, both rates are somewhat below their October levels. Although District payroll employment has not shown any real improvement, personal income tax receipts in New Jersey
and payroll income data in New York show good to moderately strong growth, suggesting that the District’s economy may be somewhat stronger than indicated by the employment statistics.

The survey of Buffalo purchasing managers showed an increase in the percentage of firms with improved new orders and/or production during December. Fifty-nine percent of the surveyed managers expect an improvement in general business conditions during the new year, compared to only 18 percent a year earlier.

Two recently announced corporate restructurings will affect District employment. In the initial implementation of its plan to cut employment by 25,000 in 1993, I.B.M. said 3000-3500 jobs will be eliminated at three of its Hudson Valley plants at the end of March. While voluntary incentive packages will be offered, layoffs may occur as well. On the other hand, a Long Island firm plans to close an out-of-District plant and consolidate its operations on the Island, adding 300 workers this year and several hundred more in the future.

Financial Developments

Most senior loan officers surveyed at small and midsized banks in the Second District indicated that their willingness to lend has not changed over the last two months. The majority of respondents indicated that overall loan demand remained slow. The demand for residential mortgages weakened as refinancing activity softened. However, the demand for commercial and industrial loans improved slightly. Almost all respondents reported that their loan rates had not changed during the preceding two months. Delinquency rates for all types of loans were unchanged to slightly lower.

With regard to recent media reports and editorials urging an easing in the "regulatory burden" on banks in order to stimulate lending, almost all loan officers indicated that capital requirements were not constraining their lending. However, several lenders at small and midsized banks suggested that reductions in the number of regulations and in the amount of time spent complying with them would permit them to initiate more loans.
Reports from business contacts in the Third District in early January indicated that economic activity was expanding at a modest rate. Manufacturers noted continuing gains in shipments and new orders and rising levels of unfilled orders. Retailers said results for the Christmas shopping period were in line with or above expectations. They reported year-over-year gains averaging around five percent, in current dollars, without significant last-minute price reductions. Auto dealers reported rising sales. Bankers generally said loan volumes outstanding were rising modestly, due mainly to growth in consumer lending.

The outlook in the Third District business community is for continued modest growth. Manufacturers forecast further expansion with some gains in employment possible by midyear. Retailers expect sales to rise during the first half but they are planning cautiously for the period. Auto dealers have a similar outlook. Bankers generally anticipate only slight growth for all types of lending.

MANUFACTURING

Manufacturing activity in the Third District continued on an upward trend as the new year began, according to reports from area manufacturers in early January. Almost half of those contacted said business was expanding while half indicated they were operating at a steady pace. Positive reports outnumbered negative ones in virtually all major industries in the District. Around half of
all the firms contacted were posting gains in both shipments and new orders, and only a small percentage were registering decreases. While around half noted steady order backlogs, those indicating rising levels of unfilled orders outnumbered those with declines by two-to-one. Although slightly more companies were hiring new workers and expanding hours than were cutting back, a majority was maintaining steady employment.

Third District manufacturers generally forecast continued expansion. Two-thirds expect shipments and orders to advance at least through June and one-third anticipate further increases in order backlogs. Although most firms indicate they will hold employment at current levels, one-third plan to step up hiring and boost hours over the next six months.

RETAIL

Most Third District retailers contacted for this report said sales for the Christmas shopping period met or slightly exceeded their expectations. Year-over-year gains averaged around five percent, in current dollars. Although some retailers said they were left with inventories somewhat above plan for the beginning of January, none expressed concern that clearance sales would have a significant negative effect on fiscal fourth quarter (November-January) profitability.

Despite the relatively good holiday sales results, few Third District retailers have expectations of strong growth in the first half of 1993. Several noted that credit card usage was high in December, and they anticipate a period of slacker sales while consumers pay down balances. In general, merchants forecast only modest growth in sales through the spring and they expect competition among stores to remain keen.
Auto dealers said sales had risen in recent weeks. They are cautious in forecasting for 1993 but believe sales for the year could exceed the 1992 level by a healthy amount.

**FINANCE**

Most of the Third District bankers contacted in early January said total loan volumes at their institutions were rising, albeit slowly. Consumer lending was most often mentioned as the strongest credit category. Several bankers said demand for auto loans and leases had increased in December and there was some carryover of the upward trend into early January. Home equity credit lines were also reported to be on the rise; however, several bankers noted that loan consolidation seemed to be motivating much of the increase as net new lending to home equity borrowers was slight. Most of the bankers contacted for this report said business loan volume outstanding was posting only sluggish growth. In general, they said demand for commercial and industrial loans was not strong, and they described loan pricing as very competitive. Most bankers also said mortgage refinancings were trending down and that the rate of growth in purchase-mortgage lending was easing.

In general, Third District bankers forecast slight growth in lending during the first quarter. They say there is little evidence that business loan demand will increase substantially and they do not expect sustained growth in consumer loan demand until employment and incomes are firmly on an upward trend.
Summary. Business activity in the Fourth District was generally stronger in recent months than was widely anticipated, and manufacturers forecast a larger increase in production this quarter than last. Consumer spending during the holiday season rose considerably more than retailers had estimated last fall, and housing sales in late 1992 showed sizable year-over-year increases. Most manufacturers of steel, autos, and capital goods forecast higher production this quarter than last. Still, businesses typically are not planning increases in employment, at least over the next few months. Lenders report a surge in credit-card use in December, but a slacker pace in mortgage loan refinancing.

Consumer Spending. District retail sales in December were much stronger than retailers expected. The surge in sales led many stores to order additional holiday-type merchandise. Despite the last-minute ordering, inventories generally have been depleted, and retailers report that heavy post-season discounting to cut excess stocks will not be necessary this year. However, traditional retailers, facing pressure from "off-price" competitors, were forced to discount merchandise prior to Christmas.

New car dealers report a mixed sales performance in December and early January. Sellers of Big Three models generally fared better than Japanese nameplate dealers, and van and light truck sales continued to grow more strongly than those for cars. Dealers claim new car inventories, in a 60- to 70-day range, are slightly larger than desired, but stocks of the new Chrysler products are said to be tight. Dealers also note that consumers are moving toward more options and high-end models within each class.

Housing and the Mortgage Market. Lenders and realtors in Cleveland, Columbus, and Cincinnati report that home sales were higher in November and December than is typical for this season. Total year-over-year sales increases in Columbus were in double digits in December, with homes priced over $250,000 posting strong year-over-year gains.
In Cincinnati, sales and starts rose at double-digit rates in November, and in Cleveland, sales rebounded after two monthly declines and were up 10% from a year earlier.

**Manufacturing.** District manufacturers expect last fall's upswing in production to continue into this quarter. Some steel producers predict that production will rebound this quarter following a decline last quarter. Several steel customers, especially automotive, have already placed orders for February and March delivery. Galvanized sheet production could reach capacity during the first quarter. Steel analysts estimate that steel operations will average about 85% of capacity this quarter, up from the 82% rate last quarter. Automotive sources also estimate a higher production rate this quarter than last. Domestic auto producers recently raised their 1993:1Q production schedules by a few percentage points from the previous forecast. If achieved, the production rate will be at least 10% higher than last quarter's pace.

Strong demand for both passenger and truck tires has pushed tire production close to capacity for some producers. According to industry sources, these producers are planning to increase capacity to accommodate the better-than-expected sales.

Capital goods producers note an uneven but steadily rising trend in their businesses. However, uncertainty over a proposed investment tax credit has led to postponements and cutbacks in some orders. A producer of information processing equipment reports that computer orders fell unexpectedly in late 1992, after a strong increase during the summer quarter. A producer of industrial motors claims that some of its customers have delayed placing new orders until more details of a possible tax credit are known.

The strongly reviving heavy-duty truck market is apparently largely unaffected by the tax credit discussion. New orders in December continue to climb at an annual rate that is well above the forecast for this year. Analysts estimate a 20% increase in output this year from last, which will place 1993 production only slightly below the level of the last peak year in 1988.
Other capital goods producers report below-average sales growth. The market for industrial controls is gradually recovering, but is still constrained by the slump in the nonresidential building industry and by weakness in aerospace. Similarly, markets for valves, fittings, and industrial components continue to strengthen erratically.

**Employment.** District employment shows little sign of a sizable pickup. Most manufacturers and retailers report that higher-than-anticipated production and sales can be accommodated with their existing work force. Although some employees have been recalled in recent weeks, many manufacturers report that they will take on new workers only after receiving sustained increases in new orders. Structural layoffs because of mergers and reorganization in the telecommunications, utilities, and plastic industries in the District are likely to result in job losses of about 1,200 workers during the year.

**Financial Developments.** Business loans outstanding rose slowly in the District again in December, according to some bankers. These sources also noted an unexpected surge in credit-card use in December. Both banks and thrifts indicate a letup in mortgage loan refinancing in December. A large thrift reported that its volume of new mortgage loans in early January had slowed substantially from a year earlier. Several thrifts and banks in the Cleveland area have been offering 30-year fixed-rate mortgages at 7.8% plus 2.5 to 3 points.
Overview

District business conditions were mostly improved during the past six to eight weeks. Retailers reported increased activity for the Christmas season. Both manufacturing and port activity held steady from the previous period. Commercial and consumer loan demand increased slightly, while mortgage loan demand declined. Both residential and commercial real estate activity increased since early November. Some District crops were threatened by unusually wet weather.

Consumer Spending

Our regular mail survey indicated that District retail activity improved in December. Retailers noted increases in shopper traffic and sales, including sales of big-ticket items. Wages and prices at the retail and wholesale levels also rose. Survey respondents reported virtually no change in employment.

Retailers were optimistic about their prospects for the next six months. They expected shopper traffic, sales, wages, and prices to rise. They anticipated profits in the first half of 1993 to exceed profits in the same period of 1992. Few retailers expected major changes in employment in their companies or in their states.

Manufacturing

Manufacturers indicated that District factory activity held steady during the past month. Respondents noted little change in most indicators, although they reported small increases in shipments, capital expenditures, and
exports. Respondents cited health care costs and government regulations as their most important problems.

Manufacturers were optimistic about their prospects for the next six months. Increases in all indicators were expected, and most anticipated a moderately lower unemployment rate in their states. Manufacturers also believed that profits in the first half of 1993 would be higher than they were in the first six months of 1992.

Ports

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated that both imports and exports remained about the same in December as in November and when compared with a year ago. Exports were expected to increase at Charleston and Hampton Roads but to remain the same at Baltimore during the next six months.

Finance

District financial institutions contacted by telephone indicated that credit conditions were varied over the last six weeks. Respondents stated that commercial and consumer loan demand improved slightly. Rates on commercial loans were unchanged, while consumer rates were lower.

Mortgage loan demand was down significantly over the past six weeks. Weakness was reported primarily in refinancings. Mortgage loan rates fell slightly.

Residential Real Estate

Real estate analysts surveyed by telephone reported that the residential market continued to improve in most of the District during the past six weeks. Residential sales increased, while home prices were mostly steady. Several respondents suggested that higher consumer confidence spurred activity in
their areas. Virtually all respondents were optimistic about real estate prospects in 1993.

The residential market in North Carolina, particularly in the Raleigh area, continued to be stronger than in other District states. Building permits strengthened somewhat in Greensboro, North Carolina, where the market has been weak for the past few years. In West Virginia, home sales continued to improve, particularly in Morgantown and the Charleston/Kanawha Valley area.

Commercial Real Estate

Commercial real estate activity increased in the past two months, according to our telephone survey of industry analysts. In some areas, vacancy rates were said to be dropping quickly. In other areas, brokers received more inquiries by businesses interested in obtaining space, and the financial condition of those making the inquiries was stronger than in prior months. The survey respondents attributed the improved conditions to increased business confidence. Most respondents said that demand was still insufficient in their markets to generate significant new construction.

Agriculture

Unseasonably wet weather continued to plague District farmers in December and early January. The harvesting of soybeans and cotton was delayed further, increasing the risk of yield losses. The wet weather assisted the emergence of small grains in the fall, but recently threatened to drown these crops in some areas. Livestock were also affected by the rains, because wet fields limited their ability to graze on small grains planted for winter forage.
Overview: According to Sixth District contacts, the Southeast economy strengthened in December and early January. Retailers enjoyed significant increases in holiday sales with claims of double-digit percentage gains over year-ago levels being common. Realtors and home builders saw continued improvement in most single-family markets. Most manufacturers reported modest increases in production and expect expansion in 1993. Bankers indicated that consumer and business loan demand is picking up. Except for some construction materials, wholesale and retail prices have remained stable and wage gains modest. Contacts across the District suggested that consumer and business confidence is reviving.

Consumer Spending: Retailers reported significant increases in holiday sales over year-ago levels and are generally upbeat about prospects in early 1993. Increased spending was noted across a wide range of consumer goods, from apparel and household textiles to big-ticket items such as electronics, appliances, and furniture. Since less price discounting was needed to move goods and seasonal hiring was conservative, retailers’ profit gains have most likely outpaced total revenues. Higher-than-expected sales have tightened inventories heading into 1993, but retailers are generally comfortable with this position. Auto sales reports were more varied, but a number of dealers reported slight increases in December from year-ago levels. They credited year-end incentive programs for the gains.

Tourism remains a bright spot in the regional economy. Contacts reported that holiday air passenger traffic, particularly international arrivals, was significantly above year-ago levels. Through year end, convention attendance exceeded 1991 levels and industry contacts indicated that advance bookings through mid-1993 promise another good year.
Manufacturing: Manufacturing activity has increased moderately in the District since late November. Production, shipments, and new orders continue to increase for textile and apparel producers. However, industry spokesmen warn that production is likely to slow since order backlogs are expected to decline by the end of the first quarter. Improving orders were also noted by contacts in industries producing electronic equipment, chemicals, and packaging.

The nation’s home-building recovery and Hurricane Andrew have resulted in gains in new orders for furniture producers, building supply companies, and lumber yards. The District’s transportation-related production has benefited from increased light truck and van sales. After struggling through most of 1992, suppliers to the offshore oil industry noted improving conditions at year end.

Construction: After taking into account normal seasonal patterns, nearly all realtors reported continued improvement in home sales. These gains were attributed to attractive mortgage rates, pent-up demand, and increased consumer confidence. Sales remain strongest in the low-to-mid price range but contacts noted increased interest in the trade-up market. Ample inventories of homes for sale kept existing home prices relatively stable, but higher lumber costs are reportedly pushing new home prices modestly higher. Although unseasonably wet weather has slowed housing starts in the District, builders are optimistic for 1993. Multifamily development remains generally weak, although scattered reports of new development in response to rising occupancy rates and firming rents are beginning to surface.

Financial Services: Most of the region’s bankers encountered improving loan demand in December and early January. Primarily reflecting increased home sales, mortgage originations were fairly strong for this time of year. Lending for autos was steady and credit card receivables
were up moderately as consumers charged some of their increased holiday purchases. Most commercial lenders also reported modest increases in loan demand, including a few business expansion loans during December. Those bankers not experiencing improvement at the end of 1992 were relatively optimistic about the first half of 1993.

**Wages and Prices:** Few factory contacts reported increases in materials or finished goods prices. Although some manufacturers intend to post modest price increases in early 1993, they are uncertain whether the increases will stick in an intensely competitive environment. There are no reports of increasing wage pressures. In fact, some major employers in the District have recently imposed moderate across-the-board wage reductions or announced plans to significantly trim current employment levels.
Summary. The Seventh District economy strengthened further in December and early January, led by consumer spending on durable goods. District retailers generally reported that holiday season sales gains exceeded expectations, and several retailers noted that sales gains held up well in the early post-holiday period. After losing some momentum in the third quarter, District manufacturing activity strengthened in November and December, particularly as motor vehicle production rose. Indicators of District employment remained mixed. The consensus forecast of a group of economists from Midwest firms called for modest but steady GDP growth in 1993, with key contributions from motor vehicles and business fixed investment, two areas important for Seventh District manufacturing activity.

Consumer Spending. District retailers generally reported better-than-expected holiday sales results, and several reports suggested that sales gains held up well in late December and early January. Responding to somewhat better-than-expected sales, a large department store chain raised its plan for first-quarter same-store sales gains to a level in line with its experience in the holiday season, and above the pace planned for the first quarter at this time last year. Another large department store chain reported that same-store sales gains in the Midwest ran roughly 5 percentage points above the national average during the holiday season. A toy retailer's sales gains in the Chicago area were significantly above its national average. An association of small retailers in Illinois reported that members' sales gains ran in the high single digits, on average, during the holiday season. An association of small retailers in Michigan stated that "our people are generally euphoric." One retailers' mail order business performed well above plan during the holiday season. This contact stated that "hopefully, we've turned the corner, but we don't want to get fooled again."

Several retailers noted that January will be a critical month for this year's plans, and sales gains appear to have held up well in the early post-holiday period. A report from a large department store chain indicated that sales growth strengthened in the last two weeks of December. A large retail chain reported that year-over-year sales gains in early January were in line with those posted in December, despite a more difficult comparison, and results in the Midwest were running slightly ahead of the national average.
Early January sales gains were led by durable goods, notably appliances, furniture, and personal computers. Another large retail chain stated that durable goods sales gains held up in early January, after a resurgence in the fourth quarter of 1992. This firm recently accelerated receipt dates for spring merchandise, which should lead to more aggressive ordering. A large discount chain reported disappointing results for early January, but was optimistic about overall consumer spending growth holding up in the first quarter.

Manufacturing. Purchasing managers' surveys and reports from individual manufacturers suggest that District manufacturing activity turned higher on a seasonally adjusted basis in November and December. In December, the overall index for the Chicago survey reached its highest level since the official onset of the national recession. The recent rebound in the overall index was concentrated in the production and new orders components, although the employment component also contributed. After slipping slightly in recent months, the price component rose in December, but remained at a level well below those experienced in the late 1980s. The director of the Detroit purchasing managers' survey characterized December's results as "no doubt the most encouraging news we've had in several years ... the economy is maintaining the recovery momentum it developed late last year." The survey's overall index remained essentially flat in December, but only after a spike in November that lifted it to a three-year high. In the fourth quarter of 1992, the strengthening in the overall Detroit index was led by responses from participants in the auto industry. A large auto producer reported that showroom traffic posted a strong increase on a seasonally adjusted basis in recent months. Citing improvement in orders from the auto industry, a steel industry analyst expected steel production to rise in the first quarter to a level 18 percent above a relatively weak year-earlier period. A machine tool producer reported some slowing in orders in recent months, but this was attributed to temporary uncertainty about prospective tax legislation. An office furniture producer stated that sales ran flat with weak year-earlier levels during recent months, but the company also reported new orders' gains and expected improved sales in the new year. An electronics manufacturer stated that orders for semiconductors from overseas markets have been holding up well in spite of slowing growth in those economies.
Employment. Alternative data sources continued to depict varying degrees of recovery in District labor markets, but the overall picture is generally one of improvement. Household survey estimates for Illinois and Michigan and local area unemployment statistics data for the other District states show a continuing recovery in total District employment in recent months. Since late 1991, when total employment (as measured by the household survey data) bottomed out, the recovery in these measures has been closely in line with the pace of the recovery from the 1981-82 recession, and total District employment now exceeds the levels that prevailed at the onset of the recession. Establishment survey estimates for Illinois and Michigan hint at a modest upturn in recent months, but the estimates for these states have been essentially flat since their recessionary lows in 1991. In Indiana, Iowa, and Wisconsin, where direct household survey estimates are unavailable, establishment survey estimates have reached and exceeded current measures of pre-recession levels. The underlying trend in the employment components of the Chicago and Milwaukee purchasing managers' surveys have followed paths similar to past recoveries. Employers continued to express concern about the impact of rising health care costs as a factor in restraining hiring and contributing to layoffs.

Economic Outlook. A reserved but optimistic mood prevailed at a recent outlook conference held at the Federal Reserve Bank of Chicago. Concerns persisted in some areas, but belief in the sustainability of the recovery seemed increasingly firmly rooted. The median forecast of 24 economists called for year-over-year real GDP growth of 2.8 percent in 1993. Key contributions were anticipated for business fixed investment and consumer spending on motor vehicles, two important sectors for District production. Car and light truck sales were forecast to rise about 10 percent to 14.0 million units in the new year, while the median forecast for housing starts called for a 12 percent increase to 1.353 million units in 1993.
Summary

District economic activity, sparked by a strong holiday sales season, continues to show signs of improvement. Holiday sales were generally strong throughout the District, and most retailers are optimistic about 1993. Manufacturers report increases in sales and employment. Single-family home construction continues to buoy the District's economy. Nonresidential construction is on the rise in St. Louis. Loans outstanding at large District banks continue to register small increases. According to District farmers, record or near-record harvests were the rule rather than the exception.

Consumer Spending

Retail sales of general merchandise in the District made a strong comeback during the holiday season. Many contacts report double-digit increases in sales compared with a year ago. Two extra days between Thanksgiving and Christmas gave retailers more time to attract early shoppers, although aggressive marketing strategies apparently were unnecessary as the level of price-cutting and advertising remained relatively low. Holiday shoppers focused on mainstays such as electronics, jewelry and small appliances, while holding off on the luxury and big-ticket items. Discounters reportedly fared better than the specialty and department stores. A number of merchants report that more customers paid for purchases with cash this year than in previous years. Inventories remain fairly steady at desired levels. Retail merchants are optimistic about the growth of sales during the early part of 1993, citing the strong holiday season and a more positive consumer attitude about the direction of the economy.

District auto sales are reported to be moderately strong, although in Arkansas, many dealers called the past quarter the worst in years. Sales of mid-sized, moderately priced cars still outpaced the sales of all others, particularly upscale models.
Manufacturing and Employment

Reports from District manufacturing contacts are more upbeat than they have been in recent months. Many speak of increases in both sales and employment. A contact in the burglar alarm industry reports that sales are up 76 percent over last year’s level. Contacts in the heavy equipment industry state that sales increased during the fourth quarter of 1992 and are expected to remain strong in the short term. Nonetheless, sales remain below peak levels, and inventories are at their lowest level since 1975-76. A beverage and grocery distributor reports that orders and inventories have been stable at desired levels. A concern of most contacts throughout the District is the lack of qualified workers available in the market. Small businesses worry about the rising cost of health care.

Other reports show District poultry producers and auto parts suppliers increasing employment because of expansions and increased demand. In addition, a major household appliance manufacturer is not only recalling 650 workers laid off during the holiday season, but expects to hire an additional 550 during the first quarter to meet demand. A District shoe manufacturer has secured a contract to begin selling its products in four major Chinese cities. A St. Louis defense contractor, however, continues to shrink with 320 more layoffs.

A recent survey of firms in the St. Louis area reveals that approximately 20 percent will hire new employees during the first quarter, while only 8 percent plan layoffs. Nationally, 17 percent of employers plan to hire, while 13 percent plan to cut employees.

Construction and Real Estate

Most areas of the District finished 1992 with single-family housing permits substantially above their year-ago levels. Homebuilders cite low interest rates, increases in consumer confidence and a surge of starter-priced housing as reasons for the continuing improvement. New and existing home sales are also up in most parts of the District; though home prices are generally flat, some increases have been reported. Contacts in St.
Louis note that nonresidential construction is showing signs of expansion, with public works projects and new factories accounting for the growth spurt. These same contacts report that the level of nonresidential construction is still running about 20 percent below the boom years of the mid-1980s.

**Banking and Finance**

Consumer and business loan demand appears to be strengthening. Loans outstanding at 12 large District banks increased 0.7 percent in November and December, after declining 0.5 percent during the prior two-month period. Business loans and consumer loans increased in November and December, while real estate loans, the largest portion of these banks' combined loan portfolio, declined 2 percent during the period after a 0.8 percent decline in September and October.

**Agriculture and Natural Resources**

Farmers reported record or near-record harvests in many areas, although some corn has yet to be harvested in the northern region of the District. While prices received by District farmers have risen somewhat recently, they remain below last year's levels. Substantial amounts of precipitation were reported in many areas of the District in late December and early January. The demand for natural gas in some parts of the District has reportedly increased markedly, owing to increased drying of the recently harvested corn crop. Cotton producers in the southern portion of the District report that the quality of 1992's cotton crop was excellent. Southern pine lumber mills report that orders have declined slightly, but that production remains substantially above that of last year.
NINTH DISTRICT—MINNEAPOLIS

The Ninth District economy continues to strengthen slowly, led by consumer spending and construction. Retail sales for the holiday season were excellent. Residential construction is much stronger than a year ago as is heavy construction. Reports on winter recreation are generally good, in spite of unfavorable weather. Labor markets show tentative improvement. Some forest products manufacturing is strong, but mining and energy production remain slow. In agriculture an extremely late harvest is now largely complete. Some farm prices have declined slightly.

**Consumer Spending**

Consumer spending in December was very strong. News media from across the district generally report strong retail sales for the holidays; several retailers described the season as the best in several years. Two Minnesota-based retailers reported same-store sales for December 9 percent and 13 percent above a year earlier.

At both ends of the district, recreation sector officials report that winter recreation such as skiing and snowmobiling is now good after late arrival of snow cover. Reports from the Upper Peninsula of Michigan describe resort and motel business above that of 1991. A Minneapolis Fed Advisory Council member reports that winter recreation businesses across Montana are having a good season in comparison to last year.

**Construction and Home Sales**

Construction, especially of homes, is strong across the Ninth District. Residential construction is reported very active in western South Dakota and Wisconsin's Chippewa Valley. The Minneapolis-St. Paul metropolitan area experienced the best growth; the number of residential building permits issued in November was nearly 52 percent above the level a year earlier. News reports from across the district note that home builders anticipate the busiest winter construction season since 1986-1987.
As in residential construction, contract awards for new roads, bridges, sewer and water projects jumped sharply in November. For Minnesota and the Dakotas such awards were nearly double those of November 1991, and the total for the first 11 months of 1992 were 17 percent above 1991. Actual construction resulting from many of these contracts will not begin until late winter or early spring.

Specific new private-sector building projects include a shopping center in Billings, Mont., an addition to a computer disk drive factory in Sioux Falls, S. Dak, and a large retail facility in Mankato, Minn. Also announced was a 100,000 square foot addition to a shopping mall in Sault Ste. Marie, Mich. Strong shopping by Canadians in this border town was reportedly a major motivating factor for this investment.

Forestry, Mining and Energy

Minnesota forestry industry officials report strong demand for lumber and for plywood substitutes, and production levels at most plants are high. A $500 million rebuilding of a plant at Cloquet, Minn., which produces a plywood substitute, is underway and will substantially increase its capacity. In contrast, the paper industry faces low prices and has slack capacity.

Metal mining continues weak. An iron mine in northeastern Minnesota sent home 600 workers for six weeks, and a Michigan mine with 700 employees shut down for two weeks. Both shutdowns were reportedly due to slack orders. One positive note was the start of work at a new open pit mine near Ladysmith, Wis. The mine, which will produce copper, gold and silver, is the first new metallic mine opened in Wisconsin in 25 years.

Oil production in North Dakota and Montana in December and for 1992 was generally unchanged from 1991. But exploration activities continue to decline; December rig counts for North Dakota and Montana were down 20 percent and 40 percent respectively from a year earlier and both are down about 60 percent from
December 1990. One exception was the announcement that a new well will be drilled in south-central South Dakota in a previously untried area.

**Labor Market Conditions**

Labor markets show tentative strengthening. Employment numbers and unemployment rates are essentially stable but initial claims for unemployment insurance fell sharply in Minnesota and Wisconsin in December.

Few large layoffs were reported in the district. A prominent Minnesota-based airline announced a nationwide layoff of over 1,000 employees, but less than 200 of these were based in the district. Layoffs of 80 and 100 workers took place at two Minnesota computer equipment firms, in addition to seasonal layoffs of casino workers. Also laid off were 30 Billings, Mont., telephone workers. But substantial hiring was reported at new businesses in Sioux Falls, S.D., as well as Eau Claire and Menominee, Wis.

**Agriculture**

The 1992 harvest is complete with the exception of about 5 percent of the corn in Wisconsin, Minnesota and the Dakotas and sunflowers in North Dakota still unharvested at year end due to unfavorable weather conditions. Overall, the crop was a record or near-record one for most grain crops in the district.

Prices received by farmers were generally steady or lower than earlier in 1992 for most major commodities except wheat. Milk prices in dairy areas are down about three percent from the previous year.
Overview. The Tenth District economy is still growing moderately. Retail sales are continuing to improve, bank loan demand is strengthening further, and farm income is rising slightly. However, while activity in the energy sector improved through yearend, some slowing is expected in the near term.

Retail Sales. Most retailers report increased sales last month, with Christmas sales strong in most merchandise categories. District retailers anticipate further improvement in sales in 1993. Overall prices increased only slightly from a month earlier and are expected to remain nearly stable. Most respondents are satisfied with inventory levels and expect no change for the next few months.

Auto sales increased slightly in the district last month, and most dealers expect this growth to continue in 1993. Some dealers report difficulty in financing inventories due to the new GMAC policy of no longer financing floor planning for autos which are not produced by General Motors. Dealers are generally satisfied with current inventory levels and expect to hold them steady.

Manufacturing. Most purchasing agents report input prices were steady to slightly higher through 1992. Prices are expected to increase only modestly in 1993. Materials are readily available although lead times are shortening in a few instances. Most firms are trimming inventories due to seasonal factors and a move to just-in-time inventory management. Firms are generally still operating below capacity. Exporting firms expect foreign sales to increase in 1993.

Energy. Drilling activity in the district continued to improve through
the end of the year. The average number of active drilling rigs climbed from 307 in November to 327 in December. The rise brought the region's rig count to a level 43 percent higher than a year earlier. Drilling activity is expected to drop sharply in coming weeks due to the yearend expiration of tax incentives for coal-seam methane gas drilling.

**Housing.** Housing starts slowed last month, due mainly to seasonal factors, but remain significantly higher than last year. Sales of new homes also slowed and the demand for mortgage funds declined as mortgage rates edged upward. Despite these developments, inventories of new homes declined last month and house prices rose. The price of lumber remains high, but prices of other building materials are about normal. Builders apparently are accepting the price increases for lumber as a permanent reality rather than an aberration to be waited out. Despite the recent rise in mortgage rates, most respondents expect rates over the next three months to stay within a narrow range.

**Banking.** Loan demand at district banks continued to strengthen somewhat last month. Demand for commercial and industrial loans was stronger at almost all banks. Demand for consumer loans and home mortgages was flat to stronger, while demand for commercial real estate loans was generally unchanged. Loan-deposit ratios were unchanged or higher compared with the previous month, but about half of the respondents reported that loan-deposit ratios were still below year-ago levels. Investments were unchanged to higher at most banks.

No banks changed their prime rates last month, and none expect to change them in the near future. While consumer lending rates were unchanged at most banks, a few respondents reported they had reduced rates. Most banks expect their consumer lending rates to remain constant over the near term. Lending standards were unchanged.
Total deposits were flat at half of the responding banks and higher at the other half. Demand deposits increased at almost all banks. NOW accounts, MMDAs, and small time and savings deposits were generally constant to up, while large CDs were generally constant to down.

**Agriculture.** Most farm operators entered 1993 in solid financial condition, and the outlook for farm income in the year ahead is relatively bright. Large supplies of corn and soybeans have pushed down crop prices, limiting prospective income gains for crop producers. But low crop prices will hold down feed costs and boost incomes for livestock producers. Overall, the outlook points to a slight gain in farm income in 1993.

District bankers expect the uptick in farm income to increase economic activity in rural communities, bolstering demand for both farm and commercial loans. While business conditions continue to improve in rural areas, many Main Street businesses are struggling to maintain sales against growing competition from national retail chains.
While District economic activity continues to grow moderately overall, signs of a slight acceleration have begun to appear in some sectors. Most prices are reported to be stable, although those of some construction-related manufacturing products have increased. Optimism is pervasive across industries. Orders to manufacturing and service firms have increased. District retail and auto sales continue to expand at a moderately strong rate in general, although retail sales along the Mexican border appear to have fallen from a year ago. Construction and real estate activity continue to pick up. End-of-year oil field activity was particularly strong but overall the energy industry remains weak. The financial industry reports rising deposits but little change in loan demand. Agricultural yields were reported as good in most areas, but prices have declined slightly.

Manufacturing activity is picking up. Production increases are greatest for construction-related products, largely because of continued expansion in homebuilding. Demand remains strong for brick, cement, lumber and construction-related fabricated metals. Prices have been increasing for these products. Demand for oil and gas-related fabricated metals remains slow overall, but foreign demand recently picked up somewhat. Production of primary metals increased slightly last month. Part of the expansion was said to reflect an anticipated January 1 increase in the price of steel. Sales of glass to automakers have increased because of an expected uptick in nationwide auto sales; prices remain stable. Demand continues to be strong for personal computers and telecommunication equipment. Orders to chemical producers are mixed. A worldwide oversupply of industrial chemicals has slowed production and held prices stable but sales of pharmaceutical chemicals are strong and prices have increased. An end-of-year surge in domestic drilling boosted demand for oil field equipment. Sales of paper products remain above last year’s level. Demand for food
and kindred products has picked up slightly. Production of denim products continues to grow at a moderate rate while producers of high-end apparel report weak sales.

The growth rate of the service activity has increased slightly but optimism has increased more. Demand has picked up slightly and some firms have increased hiring. Respondents note that they are expanding cautiously, however, and only in response to stronger sales. Prices are generally stable. District state governments face budget problems although no hiring freezes have been implemented. New Mexico is the only District state expecting a budget surplus this year. Louisiana is expecting a $900 million budget deficit and has proposed a 40 percent cut in state funding to higher education this year. The state is implementing riverboat gambling to raise revenue and produce jobs.

District retail and auto sales continue to grow at a moderately strong rate. Retailers report that prices are still competitive but inventories have been reduced without significant discounting. Wage costs are the same or lower than last year. Consumers have greatly increased credit card purchases, and one retailer speculated that this may be an indication of increased consumer confidence. District metropolitan areas, which had experienced sluggish retail sales growth throughout most of 1992, have now improved. Typically robust sales along the Mexican border, however, fell absolutely because of what respondents said was increased enforcement of import restrictions by the Mexican government.

Construction and real estate activity continue to increase slowly. Occupancy rates and rents have increased for multi-family real estate in Dallas and Austin, although rents in Fort Worth remain unchanged. New home demand is strong in Dallas, Austin and Houston. The office real estate market remains weak with the exception of Austin where rents are rising and office vacancy rates are falling. Austin is the District’s first major metropolitan area in a
decade to have office vacancy rates below the national average. While office vacancy rates are still high in Dallas, one respondent noted that prices have dropped to a point where property sales have begun to pick up. Industrial vacancy rates have fallen recently and rents seem to have stabilized after falling for the past several years.

Expiring tax credits stimulated end-of-year oil field activity but low prices and weak demand have generally slowed the energy industry. Growing world inventories have kept crude oil prices hovering around $20 per barrel. Although natural gas prices are above last year’s level, prices have weakened since October because of adequate supplies and competition from low oil prices. Some respondents expects natural gas prices to continue to decline. Refining margins remain low and profits have been estimated to be at their lowest levels since 1987. Many refineries have reduced capacity. After peaking at 935 in mid-December, the rig count ended the year just above 700 rigs, well below the 860 of 1991. A larger than normal spurt of natural gas drilling was prompted by expiring tax credits which reduced costs for wells started by December 31. A slump in drilling is certain in January, although changes in the Alternative Minimum Tax will mitigate the loss of expired tax credits.

The financial industry reports rising deposits but little change in loan demand. Refinancing on residential and commercial properties continues to boost real estate lending activity and fee income.

Agricultural respondents in most areas of the District report higher yields but lower prices. Production in 1992 will be less than in 1991 because producers planted fewer acres. Prices for most commodities are below year-earlier levels. The December Texas All Farm Products Index of Prices Received was 2.5 percent below December 1991. Prices are slightly higher for livestock commodities but lower for most crops.
Summary

Weakness in California continues to offset moderate growth in most other District states. In California, employment cutbacks continue in aerospace and defense-related manufacturing, construction, and trade. Holiday sales in California were characterized as flat to slightly improved, and the state’s fiscal outlook remains troubled. Outside of California, moderate improvement is reported in several sectors, with the strongest conditions reported in eastern Washington, Utah, and Idaho. Holiday sales were characterized as moderate to strong in most of these areas. However, the Puget Sound area faces continued uncertainty in aerospace. Overall business sentiment has improved and recent rains have improved District agricultural prospects. Little upward pressure on prices is reported and wage increases are reported to be modest.

Business Sentiment

Sentiment among Twelfth District business leaders has improved since our last report. Over half of our respondents now expect the real economy to expand during the next four quarters at a rate of at least 2.5 percent. This proportion is up from one-third in November. An additional forty percent of our respondents expect real output to expand, but at a rate below 2.5 percent.

Wages and Prices

Little upward pressure on prices is reported by contacts in most District markets. Contacts report flat prices or downward pressure on prices for new cars, air fares, furniture, paper, and computers. Aluminum prices are reported as very soft. In Oregon, a contact reports that cold weather and the closure of a nuclear power plant is causing utilities to purchase replacement power and will result in a 10 to 14 percent rise in energy prices in 1993. Another contact, however, reports that the decline in manufacturing activity in southern California has resulted in a surplus of electric
power, easing the short-term constraint in Oregon. Projections for wages in 1993 range from flat conditions to 3 percent increases, with increases in the health care industry running higher than in other industries.

**Retail Trade and Services**

Contacts from markets outside of California report good holiday sales, but less robust conditions were reported within California. Strong sales were reported by contacts in Oregon, Washington, Utah, Idaho, and Arizona. A national retailer reported a 7 to 8 percent increase in sales in the Northwest. The same retailer, however, had only a 3 to 5 percent increase in California. Another contact in California termed retail sales as "disappointing" during the holidays, with little improvement seen over 1991. A contact in small business financing reports that sales were below expectations, and that many retailers are hurting in the San Francisco Bay area.

Activity in the legal industry in California is termed weak, with several firms likely to contract employment in 1993. In addition, a telecommunications firm in California reported further deterioration in demand during November. The California governor has proposed significant cuts in aid to local governments in response to a continued state budget shortfall. The fiscal situation in Oregon is also uncertain, due to a property tax limitation and required increased spending for education. In Washington, the state has announced a budget deficit of $1.2 to $1.7 billion for the next budget cycle.

**Manufacturing**

District manufacturing activity continues to contract as layoffs in aerospace and defense-related industries continue in southern California and Washington. A manufacturer in southern California describes conditions as very bad, with no improvement in sight and further layoffs anticipated by major employers. A contact in northern California reports that layoffs are still a great concern, and that many small manufacturers are taking a wait-and-see approach to buying. In the
Puget Sound area, concern remains for additional layoffs in aerospace.

Other District manufacturing activity is showing some improvement. A contact in Oregon reports that electronics manufacturing is on the rebound. Orders for computer equipment also are reported strong for several categories, with foreign demand remaining brisk despite weakness in Japan.

Agriculture and Resource-Related Industries

Recent rains have improved the outlook for water supplies in many western states. The livestock industry is characterized as in fair to good shape, although the rain has hampered feed lots. Strong demand is reported in apple markets and rye grass seed. Wood product orders are firm, and inventory levels are low. In addition, western timber supplies are tight due to the lack of timber sales from public lands.

Construction and Real Estate

Nonresidential real estate and construction markets are reported to be weak in several District markets. One contact reports that in southern California hotel rates are declining due to increased room supply. Another contact in southern California reports that commercial rents and property values are depressed by high vacancy rates and continued employment losses. A contact from northern California reports that values of commercial buildings are falling—some below replacement cost—and that rents of some buildings are just covering operating costs.

Mixed conditions are reported in the residential sector. Housing prices in southern California continue to weaken and house prices also are reported softening in the Puget Sound area, particularly for more expensive houses. New house prices in Oregon are reported up 3 to 6 percent in smaller cities, with some lack of building lots reported due to financing constraints on developers. In Utah, housing prices are rising and land adjacent to metropolitan areas is also increasing in value.
Conditions at District financial institutions are reported as mixed. Outside of California, contacts report some growth in loan demand and deposits in Arizona, Utah, and Washington.

In California, contacts report that loan demand remains weak and that the volume of outstanding loans continues to decline. Asset quality is reported weak as well, although one contact reports that the pace of deterioration has slowed recently. One contact reports that the overall delinquency rate decreased for November. Some increased demand is reported for residential mortgages and home equity lines of credit.