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Summary of Commentary on

Current Economic Conditions

by Federal Reserve District

October 1999

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SUMMARY[1]

Most districts continue to report strong economic growth but some slowing is noted. Manufacturing activity continues to advance in almost all districts and for most industries. Although four districts report some slowing in consumer outlays, spending generally remains strong and most retailers are expecting increases in holiday sales from last year. Real estate and construction are still robust in most districts, though there are signs of some moderation in activity. The mining and energy industries are showing signs of recharging. Overall loan demand remains brisk, although a softening is noted by some districts in consumer loan demand. Labor markets remain tight across the country, with numerous districts reporting continued difficulty in finding and retaining qualified workers. Many districts report a pickup in wage increases, but overall prices remain stable with some notable exceptions: Increases in prices were noted for some manufacturing inputs, health care, memory chips and construction materials. By contrast, low prices continue to weigh heavily on some important segments of the agricultural sector.

Consumer Spending

Many districts report continued steady to strong retail spending, while the Chicago, Dallas, Kansas City and New York districts mention weakening sales. The Minneapolis and San Francisco districts report sizable increases in sales; in the Philadelphia district, several stores experienced double-digit increases over last year. Sales growth in the Boston district is generally exceeding retailers' expectations. But retailers in the Kansas City district report a decline in sales, following flat activity in the three previous surveys. Most districts note that retailers expect strong consumer demand as the holiday season approaches. Auto dealers report solid sales in the

[1] Prepared at the Federal Reserve Bank of Minneapolis and based on information collected before October 25, 1999. This document summarizes comments received from businesses and other contacts outside the Federal Reserve System and is not a commentary on the views of Federal Reserve officials.

Dallas, Kansas City and Philadelphia districts, with weakening demand indicated in the Chicago district. In the Cleveland district, auto sales slowed in October after a record summer. Some dealers continue to have short inventories of some popular models. Fall tourism is steady compared to a year earlier in the Minneapolis district. Hurricane Floyd depressed tourism at coastal destinations in the Richmond district, but inland mountain resorts report gains.

Manufacturing

Nearly all districts report that manufacturing activity is growing. The Boston district reports most suppliers to the semiconductor, telecommunications, biotech and construction industries are experiencing double-digit increases in business. Several manufacturers of industrial products and chemicals in the Philadelphia district note increases in orders from customers in Asia. The Richmond district reports that shipments and capacity utilization levels are increasing; production was particularly strong in printing and publishing. Shipyards in Louisiana are operating at full capacity, according to the Atlanta district. The Chicago district reports that automobile production was steady at very high levels in recent months. Strong growth in sales of plastics and building materials is reported by the St. Louis district. The Dallas district reports a slight increase in manufacturing activity. The San Francisco district reports expansions in petrochemical production, paper processing, steel manufacturing and high-technology equipment manufacturing.

Kansas City is the only district reporting a slowing in overall manufacturing activity. In addition, the Boston district notes that production of industrial machinery and machine tools remains below year-earlier levels.

Moreover, several districts report selected price increases: health care costs (Atlanta, Chicago and Minneapolis), memory chips (Dallas), paper (Minneapolis) and construction materials (Atlanta and Minneapolis). In contrast, the Dallas district reports the prices of lumber and wood products and cement have declined recently.

Real Estate and Construction

Real estate and construction remain robust in most districts, though indications of some slowing have surfaced recently. Residential real estate activity is at high levels in the Richmond and San Francisco districts, although the pace of growth is slowing. In the Boston, Chicago and Kansas City districts recent interest rate increases have curbed home sales. Existing home sales rose just 1 percent in September in New York State, but prices increased 6 percent from a year earlier. In the Kansas City district building activity improved following several months of decline, but was flat compared with a year ago. Housing units authorized are above year-earlier levels in the Minneapolis and St. Louis districts.

The commercial real estate markets are considered tight in several districts and commercial construction is increasing. The Chicago, New York and Richmond districts report low office vacancy rates. The pace of construction is slightly ahead of a year ago in the Atlanta district, but the level of activity was uneven across the district.

Most districts report that residential and nonresidential construction is constrained by labor shortages and higher prices on some construction supplies. The St. Louis district notes that shortages of workers and certain materials will continue to delay some projects.

Banking and Finance

Most districts report increases in overall loan demand, although four districts indicate some easing in the demand for consumer loans. The Cleveland, New York, Richmond and

Chicago districts report a softening in consumer loan demand. Only the New York district experienced weakness in overall loan demand. Commercial lending activity increased in the Philadelphia, Richmond, Chicago and Kansas City districts. The Richmond district reports that commercial bank lending is driven by continued business expansion and, in some cases, the anticipation of higher interest rates. Consumer lending has strengthened in the Philadelphia, Atlanta, St. Louis and Kansas City districts. Credit quality is good in the Atlanta district, and bankruptcies continue to gradually decline. The San Francisco district reports continued solid credit quality, while in the St. Louis district many bankers are becoming increasingly concerned about delinquency rates and have upped their loan loss reserves accordingly. The New York district reports tighter credit standards for all categories of loans.

Agriculture and Natural Resources

Most of the country is having a good harvest. The Chicago, Cleveland, Kansas City and Minneapolis districts all report good harvest conditions for their crops. Record soybean and sugar beet crops are projected for some states. Drought has reduced yields in the Dallas, Richmond and St. Louis districts, but hurricanes brought much-needed rain to most areas of the East Coast and too much rain in some areas. The San Francisco district reports mixed agricultural conditions, with good conditions for fruits and rice, and poor conditions for vegetable and grain producers. Farm income, however, remains depressed as dismal agricultural prices are offsetting the bumper crop.

Conditions for dairy producers remain strong, report the Cleveland and San Francisco districts. Meanwhile, cattle and swine herds have benefited from low feed prices. The Kansas City and San Francisco districts report favorable conditions for cattle ranchers; however, the Chicago district reports a sharp decline in the size of the swine breeding herd. The Dallas district reports most pastures had limited forage for livestock, and supplemental feeding and herd reduction continued in most areas.

Oil exploration is on the rise, with oil rig counts in the Dallas, Kansas City and Minneapolis districts higher than early summer levels. In addition, the Minneapolis district reports several iron ore mines restarting taconite production.

FIRST DISTRICT-BOSTON

Business activity continues to expand at a vigorous pace in the First District. Retail sales are expanding solidly and most manufacturing contacts' revenues are up. Retailers, with one exception, say their vendor and selling prices are steady or even declining, while half the manufacturing respondents report rising materials costs. Labor costs may be accelerating somewhat, with manufacturers offering attractive recruitment packages and slightly higher wage increases while retailers engage in more raiding. In addition, manufacturers express concern about sizable projected increases in the cost of medical benefits.

Retail

Most retail contacts report solid sales growth during the months of July through September. These growth figures, in the middle single-digit range, are generally better than sales projections for the period. Inventories are considered to be at desired levels. Looking forward, retailers are optimistic that consumer demand will remain strong through the important Christmas period.

Employment is said to be holding steady. Most retail contacts continue to say that wages are growing at a 3 to 5 percent pace. All respondents indicate that the labor market is very tight and some are having difficulty finding temporary help for the Christmas season. In contrast, contacts are having no difficulty hiring or replacing permanent help, although raiding is reported to be more common. Most retail respondents say that consumer goods price inflation is non-existent and that vendor prices are either holding steady or declining. By exception, hardware prices are increasing because of manufacturers' price increases. Gross margins are said to be holding steady.

Retailers are planning modest capital expansions for next year. Most contacts say that economic fundamentals are strong and hence they expect steady economic growth to continue for the next six months. Respondents in the interest-rate-sensitive construction supply business report that building contractors indicate they have orders booked for the next six to nine months.

Manufacturing and Related Services

Three-quarters of First District manufacturing contacts report that recent business is up relative to a year ago. Most suppliers to the semiconductor, telecommunications, biotech, and construction industries are experiencing double-digit increases in revenue; otherwise, gains tend to be more modest. Manufacturers of aircraft components report moderate to weak demand. Production of industrial machinery and machine tools remains below year-ago levels. Competition from imports has forced the closure of some plants in the apparel textile and paper industries.

One-half of the manufacturers contacted indicate that materials costs are rising. The most commonly mentioned increases are for fuels, plastics, and petrochemicals; copper and aluminum; and paper and cardboard. Selling prices are said to be mostly flat. However, some companies are raising their prices in response to higher costs for materials and labor, while manufacturers of automotive and aircraft equipment report that their customers are continuing to press for price reductions.

Most manufacturing contacts report steady or rising headcounts, although some large firms have instituted layoffs. Average pay increases are said to be in the range of 3 to 6 percent. One-quarter of the respondents report that production worker turnover is their most serious problem; they are offering a variety of bonuses, compensation adjustments, and flexible work schedules to attract and retain labor. Many companies expect double-digit increases in health care premiums for next year; some express concern about the need to restructure benefits.

Most manufacturers expect their revenues to increase in 2000. Many cite evidence of turnaround in Asia as a contributing factor. By contrast, sentiments regarding the U.S. economy have become more mixed and some contacts have become more proactive with respect to managing their outlays. The century date change appears to be having only a minimal effect on most manufacturers' projections.

Residential Real Estate

Real estate contacts say that higher interest rates somewhat diminished demand for real estate in New England during the past quarter. The effect of higher interest rates is especially visible in lower demand for newly built high-end homes in some greater Boston communities. Most respondents report that markets are still strong, however, and low inventory continues to be the major problem in many areas. Third quarter sales were comparable to the same period last year and most contacts report modest price appreciation. Massachusetts contacts indicate that price growth has slowed in 1999 compared with its 1998 pace. The market is viewed as "more normal" now than it was during the previous couple of years. Connecticut continues to be identified as the weakest residential market in New England, although contacts there report steadily improving conditions, with modest price appreciation and lower inventory than a year ago. Contacts expect modest price appreciation to continue but anticipate a seasonal slowdown in sales until February or March.

Investment management

Investment management contacts in the First District report that total assets under management decreased in the third quarter because of the reduction in the market values of equity. Nevertheless, respondents continue to expand employment in the areas of customer service and technology, areas in which labor market tightness persists.

SECOND DISTRICT--NEW YORK

Economic growth in the District has shown signs of slowing since the last report, with some softening in consumer demand accompanied by ongoing labor shortages. Consumer price inflation remains subdued, despite indications of increased cost pressures—prices of manufacturing inputs continue to rise, and a large employment agency reports an acceleration in wages. Retailers indicate that sales were on the weak side in September and the first three weeks of October. Homebuilders and realtors in the New York City area report that markets are still strong but have cooled a bit since the summer. New York City area office markets remain tight, while rents have risen modestly.

Regional purchasing managers report that manufacturing activity was mixed to weaker in September while cost pressures intensified further. Banks report a decline in loan demand and a noticeable tightening in credit standards, accompanied by continued improvement in delinquency rates.

Consumer Spending

Retail sales have been mixed but, on balance, slightly below plan in recent weeks. A majority of retail contacts report that sales growth slowed in September and picked up only modestly over the first three weeks of October; on the other hand, two large chains report that business has been fairly brisk. Some retailers with sluggish sales blamed part of September's weakness on mid-month flooding from Hurricane Floyd, though that was not viewed as the major factor. In general, sales of consumer durables—home improvement, electronics, appliances, etc.—were said to be on the strong side, while apparel sales tended to lag. Despite the modest slowing in sales, inventories are generally said to be at satisfactory levels. One large chain reports that its greatest concern is having adequate inventories on hand by Thanksgiving weekend; while shipping delays appear to be much less of a problem than last year, there are reports of minor bottlenecks at West Coast ports.

Selling prices and merchandise costs are reported to be little changed, on balance, in recent weeks. However, a number of retailers say that the pricing environment for the upcoming holiday season is shaping up to be more competitive than last year; one retailer indicates that some competitors have already begun discounting merchandise. Wage pressures remain steady thus far, though a number of contacts are concerned that they may intensify as seasonal hiring picks up in November.

Construction & Real Estate

There are signs that the region's housing market has cooled somewhat from this summer's torrid pace. In New York State, sales of existing single-family homes slipped in September, and were up just 1 percent from a year earlier; however, prices were up by a brisk 6 percent from a year earlier, led by double-digit gains across most of the New York City area. Based on anecdotal reports, part of the weakness in unit sales may reflect a dearth of homes on the market. In Manhattan's co-op and condominium market, a major realtor reports that demand remains exceptionally strong, and that there has been a recent increase in new listings—more people putting their homes on the market.

New Jersey homebuilders report continued strong demand for both new and existing homes. There continues to be an unusually long delivery time for new homes, reflecting shortages of both materials and workers. An industry expert indicates that homebuyer traffic was affected by severe weather in September, but otherwise has remained brisk; however, he notes that there now seems to be less of a sense of urgency to buy than a few months ago.

Office markets across most of the New York City area remain tight as a drum. Office vacancy rates across Manhattan continue to hover at cyclical lows. Office rents in Midtown and Downtown have risen only modestly this year, but rents in the Midtown South area (including Silicon Alley) continue to rise at a double-digit rate. Office vacancy rates in Westchester and Northern New Jersey edged down in the third quarter, while Long Island's vacancy rate fell sharply, to a cyclical low of 7.1 percent.

Other Business Activity

Regional purchasing managers' surveys for September indicate a mixed but generally weaker picture of the manufacturing sector, along with heightened cost pressures. Buffalo purchasers indicate steady growth in new orders and a further acceleration in production activity in September, along with persistent but steady increases in commodity prices. Purchasing managers in both the New York City and Rochester areas report a downturn in manufacturing activity, along with increasingly broad-based inflation in input prices.

There is some anecdotal evidence that the slowing in regional payroll employment growth in the third quarter may reflect labor shortages. A large employment agency reports that demand for temporary workers remains strong but that "effectively, there are no more temps." The contact describes the labor market as very tight and notes that the current lack of contingent workers is now "driving up salaries and fees in full-time job placement." There has been a pause in demand for computer specialists, as Y2K needs are slackening, but strong demand is expected to resume next year. Separately, a recent survey of the securities industry indicates that technology spending is expected to increase by 7 percent annually over the next three years—largely to support on-line investing.

Financial Developments

Demand for loans weakened since the last report, according to bankers at small and medium sized banks in the District. Approximately two in five bankers report lower demand while only one in five indicate higher demand. The weakness in demand was most pronounced in the consumer and residential mortgage segments. Refinancing activity continued to slow, with half of the bankers surveyed reporting declines.

On the supply side, bankers report tighter credit standards for all categories of loans—particularly on nonresidential mortgages and commercial and industrial loans. A large majority of bankers raised rates on both loans and deposits since the last report. Finally, delinquency rates continued to drop in all loan sectors, led by residential and nonresidential mortgages.

THIRD DISTRICT – PHILADELPHIA

Third District business activity continued on an upward path in October. Manufacturers had increases in shipments and orders, and they reported stepped-up demand from Asian customers. Retail sales continued to grow at a solid rate. Auto sales have been steady. Bankers reported modest gains in consumer and business lending, but a slowing in residential mortgage activity. Both manufacturers and retailers indicated that they are having difficulty finding workers, both skilled and unskilled, and that wages are rising. Service firms, with the exception of health services, also said they are having difficulty finding new employees. Some business contacts said that it is taking longer to fill open positions now than it did a year ago.

Looking ahead, businesses in the Third District generally have optimistic views, although they caution that their expectations could change if financial conditions become less positive. Manufacturers expect shipments and orders to continue growing at their current rate, but they are concerned that costs will rise as well. Retailers expect a good pace of sales in the fourth quarter, but they predict a consumer pullback if interest rates rise further. Bankers expect lending to continue moving up through the end of the year, but at a slower pace.

MANUFACTURING

Manufacturers in the Third District reported moderate growth in October, on balance. While half of the firms contacted said shipments and new orders were steady during the month, one-third said they had increases. Gains were common among all the major industrial sectors in the region. Several manufacturers of industrial products and chemicals noted increases in orders from customers in Asia. Despite the increase in orders in October, most of the firms polled during the month reported that order backlogs were steady.

Employment at plants in the region has been virtually level. Several companies indicated that shortages of both skilled and unskilled workers have restricted their ability to respond to increased demand for their products. One firm reported that it recently established a plant overseas because of its inability to find more workers in the U.S.

Reports of rising costs for raw materials and supplies have become more common from Third District manufacturers. In particular, producers of chemical, food, and paper products indicated that prices for the raw materials they use have begun to increase. However, according to the firms contacted for this report, competition among firms is still keeping output prices in check, putting pressure on profit margins.

The outlook among manufacturers in the region is positive, although there is some concern regarding rising input prices. On balance, managers at area plants expect the current rate of growth in shipments and orders to continue over the next six months. They are seeking more workers, and they are planning to increase capital spending. Nearly half of the firms contacted anticipate increases in input costs, and half expect costs to remain near current levels. One-fourth plan to raise prices for the products they make, but over half will keep prices steady.

RETAIL

Retail sales in the Third District continued to move up at a good pace in October, according to merchants interviewed for this report. Several stores indicated that their recent year-over-year sales comparisons have been in excess of 10 percent, in current dollars. Fall apparel has been selling well, as have other seasonal items. Some stores noted a pickup in sales of camping and outdoor goods to customers who fear interruptions in utility services due to Y2K problems. Inventories were generally described as in line with plans, although a few merchants indicated their inventories were somewhat below desired levels. Reports of labor shortages have become common among the region's retailers, who anticipate some difficulty in fully staffing their stores for the holiday shopping period.

Auto dealers generally said sales have been running at a high, steady rate in recent weeks, although some noted slight easing. Inventories were in line with sales at most dealers, but several noted that the supply of popular models has not kept up with demand.

Looking ahead, most store executives expect a strong fourth quarter. Some expressed concern that recent increases in interest rates and volatility in financial markets could trim consumer confidence, but most area retailers said they have seen no sign of a slowdown in spending yet. Similarly, auto dealers believe sales will remain at or near the current pace as long as consumer confidence does not weaken.

SERVICES

Business continued to be good for the region's law firms and other business service firms. Service companies are adding workers in a variety of specialty occupations and basic clerical positions. Information technology professionals remain in high demand. However, hospitals and health services firms have laid off workers recently.

FINANCE

Lending officers at Third District banks generally reported modest growth in lending in October. Lending to individuals for consumer purchases has picked up recently, but home mortgage lending appeared to be slowing. Bankers said lending to businesses was moving up slowly. Lending officers noted that some of their business borrowers were not achieving the growth they had been expecting. Partly in response to this development, some banks said they were reviewing credit standards for commercial and industrial loans and planned to make them more stringent. Nonetheless, several bankers said lending for commercial real estate from a variety of financial firms was still aggressive in the region.

Looking ahead, most of the bankers contacted for this report expect consumer borrowing to pick up seasonally, but they expect some slowing in growth in other credit categories. Concern about liquidity at the turn of the year appears to be growing. Several bankers said they were receiving inquiries about expanded credit lines for December and January from current business and local government borrowers who are concerned about payment interruptions due to possible Y2K problems. Bankers also said they are concerned that depositors' demand for currency will rise significantly as the year comes to a close.

FOURTH DISTRICT - CLEVELAND

General Business Conditions and Labor Markets

Business activity in the Fourth District remains strong, and some upward pressure in wages continues to be seen. Larger price increases are noted for certain commodities in the industrial sector, but retail prices remain steady.

District temporary employment agencies reported continued high demand. All contacts face ongoing difficulty finding and retaining qualified workers. Agencies noted that, increasingly, firms are retaining temporary employees on a permanent basis, and in an effort to attract new workers, the agencies have had to raise wages. Rising wages have helped entice some workers back into the job market; a technical training center in Columbus reported that retirees make up a large share of its computer education classes.

Due to the upcoming holidays, there has been a large increase in demand for workers in customer service, warehousing, and distribution. Sources anticipate that the demand for temporary retail workers during the holiday season will be even greater than last year's record-high level.

Wage growth is inching up in almost all industries covered by collective bargaining agreements, averaging around 3 ½%. Job security and benefits remain top priorities, and several contacts reported "dramatic" increases in pension benefits; minimum pension contributions have more than doubled in the past year for some employers.

Construction

Persistent labor and materials shortages continue to plague commercial builders, with contacts noting backlogs of 30 to 45 days for some materials—a significant increase from earlier in the year. Nevertheless, labor and materials costs remain relatively flat.

Most commercial builders noted improved sales activity within the past six weeks, compared with earlier in the year. Particular strength was noted in the Cleveland and Columbus metropolitan areas; some weakness was reported in Cincinnati.

For the first time in recent memory, residential builders are beginning to report a softening in sales volume, with sales in the third quarter of 1999 reportedly down about

10% from the previous quarter. The recent slowdown in the pace of residential construction is generally being blamed on higher mortgage interest rates.

Unlike commercial builders, residential contractors reported that materials and labor costs are still increasing—each is estimated to have risen 3% to 5% year-to-date. Materials and labor shortages have also resulted in longer orders backlogs.

Agriculture

Crop yields were extremely varied across the District in 1999. In the northern reaches of the District, corn and soybean harvests were average, or slightly less than average. However, reports from southern Ohio and Kentucky indicate crop harvests were 50% to 85% below average.

Recent rainfall in the District has helped the winter wheat and tobacco crops. Most tobacco is reportedly in good or fair condition, although yields are below average. The dairy industry is generally doing well throughout the District. Milk prices remain high, and feed prices have come down from earlier in the year. In some areas, recent rainfall has renewed pasturelands that had been diminished by earlier drought conditions.

Industrial Activity

Industrial activity is holding steady or growing moderately in the District. Production and orders data are generally favorable, and inventories have come down somewhat from the summer. Basic commodity prices are rising, a trend that appears to have begun this summer. Prices were noticeably higher for steel and paper goods and some chemicals. Shortages are seen for a variety of skilled trades, but wage growth is said to be modest.

Capital goods producers continue to see high production levels and a strong orders pace. Auto-related manufacturing remains exceptionally strong. Some slowing in the heavy truck market has been seen, and the orders backlog—which had extended to about a year this summer—has been reduced by about one-third. Still, orders and production in this industry remain somewhat high by historical standards. Agricultural equipment production remains flat.

Most steel companies in the District report poor third quarter earnings, primarily attributable to low prices. Mergers and acquisitions are believed to have deflated the earnings reports a bit. Strong demand and firming prices are expected to improve conditions in the industry slightly this quarter.

Consumer Spending

Retail sales are still showing strong gains overall, although a few retailers have seen some softening in the first few weeks of October. Sales in August and September ranged from good to better, with exceptional sales reported for apparel stores.

General merchandise inventories are low, but most retailers reported plans to steadily increase stocks in preparation for the holiday season. Some also indicate a desire to stockpile larger-than-usual inventories as a precaution against possible Y2K-related tie-ups in the supply chain.

Despite the continued strong sales pace, retailers report steady prices and a very competitive sales environment. Retailers also indicate having difficulty finding workers and are anticipating labor shortages as the holiday shopping season approaches.

Sales of new vehicles slowed in October, after record sales over the summer. All dealer contacts reported missing their October sales projections, although year-over-year sales are still up sharply—between 5% to 15% from last October. The 2000 model year is selling well, and most of the 1999-model-year stocks have been liquidated. A few shortages of some 2000 year models were noted.

Banking and Finance

Lending activity in the District is generally down from the last District report. Most banks are reporting difficulty attracting deposits as people move available funds into equity markets. The loan-to-deposit ratio has risen, reducing banks' ability to lend, and some sources indicate having tightened credit standards. Higher interest rates have dampened credit applications somewhat.

Loan delinquencies are holding at a low level and credit quality is high. The spread between borrowing and lending rates is narrowing in accordance with the observed long-term trend.

FIFTH DISTRICT – RICHMOND

Overview: Fifth District economic activity advanced at a solid pace in late September and October, despite some easing of growth in interest-sensitive sectors. Retailers reported stronger sales and a pick-up in employment while manufacturers recorded moderate gains in shipments and an increase in capacity utilization. The services sector reported modest growth in revenue and employment outside of finance and real estate. At financial institutions, commercial lending remained strong, but residential mortgage lending flagged. Real estate activity was mixed; both residential and commercial markets remained buoyant, although growth slowed in some areas. Wage growth strengthened further in many sectors of the economy, while price increases remained generally subdued. In agriculture, a series of hurricanes in September and October brought heavy rain and flooding in eastern regions of the District, and slowed the planting of small grain crops in Virginia and North Carolina.

Retail: Retail sales growth exceeded expectations in late September and October. Furniture sales were particularly robust, driven in part by homebuyers moving up to larger homes in recent months. A retail stock analyst in Richmond, Va., stated that back-to-school sales were strong in September, and predicted that solid sales growth would continue into the upcoming holiday season. District retailers anticipate good holiday sales and a number have stepped up hiring much earlier than usual in an attempt to "beat the rush" for holiday sales help. Wage growth picked up noticeably as retailers sought to expand payrolls, but retail price increases remained moderate.

Services: Revenue growth in the services sector has been spotty since our last report. Business services revenues were generally higher, especially in Richmond, Va., and Charlotte, N.C. However, growth in finance and real estate activity was trimmed by anticipations of higher interest rates, and many restaurant and entertainment businesses in coastal areas of North Carolina and Virginia experienced sales declines in the aftermath of Hurricane Floyd. In addition, brisk sales of new cars slowed revenue growth at automobile repair shops; one South Carolina contact remarked, "No one needs to fix a car when they're all brand new." Employment at services producing firms was flat since our last report, while substantial wage growth persisted.

Manufacturing: District manufacturing activity generally grew at a moderate pace in September and October, even though softness remained in some industry segments. Shipments and capacity utilization levels increased; production was particularly strong in the printing and publishing, fabricated metals, industrial machinery, and rubber and plastic industries. A North Carolina producer of industrial machinery said that his company had recently scheduled an additional shift because of a surge in its custom fabrication business. In contrast, textiles and apparel producers continued to report weak demand and production overcapacity--particularly in denim lines. According to a North Carolina producer, excess denim manufacturing capacity has caused a "price war" for those product lines. He expected six months or more of difficult market conditions ahead. In labor markets, manufacturing employment and wage growth held steady, while the average workweek fell. Prices paid for raw materials rose, in part because of substantial increases in petroleum prices.

Finance: District bankers reported that commercial loan demand remained strong in September and October, while the demand for home mortgages eased. Commercial bank lending was driven by continued business expansion in the District and, in some cases, the anticipation of higher interest rates. A Charlottesville, Va., banker noted that his commercial business borrowers were securing loans now, "before rates go up further." Although mortgage rates have not advanced substantially since our last report, mortgage lenders indicated that earlier rate increases had cooled loan demand. Mortgage refinancings, in particular, were down considerably. Competition for residential mortgage customers intensified; a banker in Greenville, S.C., noted that he was seeing more competition from lending affiliates of large national home building firms.

Real Estate: Residential real estate activity in the District remained at a high level, although the pace of sales activity eased in recent weeks. Realtors said that people are taking a little more time to purchase a house now, and, in the words of a central North Carolina realtor, "...are looking for less house." Some of the slowdown in that state can be attributed to Hurricane Floyd, which slowed real estate activity in eastern North Carolina but had little effect on markets in other areas. Shortages of labor and building materials persisted in some areas, but wallboard was said to be somewhat more available. Construction labor costs rose slightly, especially in the Tidewater Virginia area.

Commercial real estate activity was mixed since our last report. A contact in southern Maryland reported a slowdown in office and retail leasing; in contrast, a realtor in the Maryland suburbs of the District of Columbia said any Class A office space coming on the market was pre-leased. A realtor in Charlotte, N.C., told us that office construction continued in suburban areas, and that the supply of Class A office space was tight downtown. Vacancy rates generally changed little, except in Richmond, Va., where realtors reported that Class A space was being "eaten up," by a large financial services company.

Tourism: Tourist activity strengthened in mountain areas of the District but weakened along the coast after three hurricanes brought extensive flooding to coastal areas. A contact on the Outer Banks of North Carolina reported a decline in bookings in both September and October and noted that tourist activity had simply lost momentum in the aftermath of Hurricanes Dennis and Floyd. A Virginia Beach hotelier reported a 16 percent decline in occupancy due to inclement weather. Resorts in mountain areas, however, benefited from the storms; a contact at a mountain resort in Virginia reported that tourism in that area strengthened as vacationers escaped the battered coast and headed for the mountains.

Temporary Employment: The demand for temporary workers remained high since our last report, while the supply of qualified workers shrank further. Contacts in Virginia and the Carolinas reported increasing turnover among temporary employees as these workers pursued higher paying job opportunities. Wages for temporary workers rose at a faster pace since our last report, but wage growth was not expected to accelerate substantially in coming months.

Agriculture: The hurricanes brought heavy rains to farmland in most of the District. With the exception of West Virginia, soil moisture levels are now generally either adequate or surplus. In addition, the recent weather conditions were favorable to the fall planting of the Maryland, West Virginia, and South Carolina small grain crops. In contrast, wet fields continued to hamper planting of small grains in Virginia and North Carolina. Peanut harvesting activity is behind schedule in Virginia and the Carolinas, as is the harvesting of cotton. Wet weather also led to a poor pumpkin crop, as the gourds rotted in many fields. Pasture and livestock conditions continued to improve in South Carolina and Virginia, but remained poor in West Virginia.

SIXTH DISTRICT – ATLANTA

Summary: The southeastern economy posted mixed growth into fall, and the outlook remains mostly upbeat. Merchants' sales have, on balance, met expectations, and contacts anticipate that fourth quarter sales will outpace those of a year ago. Residential construction and sales were nearly unchanged from the previous month, while commercial building was ahead of last year in most markets. Advance bookings for the tourism and hospitality sector are disappointing in parts of the District. Overall manufacturing activity increased recently, but weakness persists in certain sectors. Bankers report mostly strong loan demand. Tight labor markets continue to plague District employers, but there are few reports of accelerating wage pressures. Prices remain stable, with a few exceptions.

Consumer Spending: Sales results during September and early October have been decidedly mixed as about half the retailers contacted said sales were down from a year ago, while the remainder experienced increases. However, most merchants said that recent sales have met their expectations and inventories are balanced. The strongest sellers recently have been women's and children's apparel, while home-related product sales have varied across the region, and men's apparel sales have made a poor showing. Looking to the fourth quarter, a majority of retailers anticipate sales will be up slightly compared with last year.

Construction: The pace of single-family construction in October was similar to September, while new home sales weakened. Reports indicate that construction levels are especially weak in Louisiana and Mississippi. Realtors indicate that new and existing home sales in September and October have been mixed across the region with a slight improvement noted in October. The majority of contacts said that home inventories are currently balanced.

Looking forward, most builders expect construction levels to be similar to, or slightly below, last year's levels through the end of the year. The pace of District multifamily construction remains similar to our last report, up modestly from a year ago.

The pace of District nonresidential construction is slightly ahead of a year ago but varied across the different states in the District. Contacts in Florida, Georgia, and Tennessee report that construction continues to slow but remains above year-ago levels. In Louisiana, construction activity is similar to last year's level, while in Alabama and Mississippi construction continues at below year-ago levels. Vacancy rates are on the rise in the Atlanta office and industrial markets as well as the Orlando office market.

Manufacturing: Manufacturing activity increased moderately since the last Beigebook. Most contacts noted increases in production and new orders; reports pertaining to the near-term factory outlook were also positive. New military weapons contracts are expected to boost employment rolls in Mississippi and Alabama. Shipyards in Louisiana are reportedly operating at 100 percent capacity because of large long-term contracts. Stabilizing paper costs are helping District printers, but there is concern about business loss to electronic media. Less positively, the factory workweek and shipments are declining for an appliance producer, perhaps indicating some slowing from national residential housing markets. Several contacts said that hurricanes caused lost factory production days in the District. However, demand increased for lumber and wood products because of storm damage repair.

Tourism and Business Travel: The outlook for the tourism and hospitality industry, while good, is a little less positive than before. Some south Florida resort and hotel owners are disappointed with advance bookings for the upcoming tourist season and are pessimistic about exceeding last year's results, speculating that some tourists are reluctant to make plans until after Y2K. Bookings for the "Turn-of-the-Year" are said to be disappointing. In Atlanta, 1999 is reportedly shaping up to be the best year the city has ever had for conventions, but bookings are down for the year 2000 partly because of competition from other cities with new or expanded facilities. Gaming revenues along the Mississippi Gulf Coast are at record levels and are expected to outpace those of a year ago by double-digits.

Financial: Bankers report that overall loan demand and lending remains strong throughout the Southeast. Consumer and automobile lending remain very strong, commercial lending has moderated, and mortgage and refinancing loan demand are subdued. Banking contacts around the District report that credit quality is good, and bankruptcies continue to gradually decline; however, there were reports that some bankers are showing an increasing willingness to accept higher risks in making loans and are making some concessions on loans and borrower qualifications.

Wages and Prices: Contacts continue to note problems with tight labor markets, but there are few reports of accelerating wage pressures. One contact reports that the use of excessive overtime to make up for labor shortages is causing morale and productivity problems. Competition for new and replacement employees is reportedly intense in Miami, Jacksonville, New Orleans, Atlanta, and Nashville. Skilled construction workers, nurses, and information technology professionals remain in especially high demand.

Contacts expect no significant changes in the prices of inputs or outputs for the near term with only a few exceptions. Health insurance premiums and pharmaceuticals prices are expected to continue on an upward trend. Some contacts say that the cost of higher oil prices is cutting into profits more than impacting the pricing of goods and services because of the competitive marketplace. An "abundance of work" is keeping construction materials prices high in parts of the District.

SEVENTH DISTRICT—CHICAGO

Summary. The Seventh District's expansion appeared to slow modestly in September and early October as consumer demand moderated. Retail sales were below what most retailers had expected and reports from District auto dealers became mixed. Construction and real estate activity slowed on the residential side, but most contacts indicated that the market was still "healthy." Manufacturing activity was steady at very high levels of production. Overall loan demand remained strong, despite some softening on the consumer side related to slowing in mortgage lending. Labor markets appeared to tighten further and reports of intensifying wage pressures became more frequent. The fall harvest was proceeding rapidly thanks to dry weather, and yields were turning out better than many had anticipated. District hog farmers reduced the size of their breeding herds relatively more than farmers in other states.

Consumer spending. Overall consumer spending slowed in September and early October, with sales results falling below most merchants' expectations. Many contacts suggested that warmer-than-usual temperatures negatively impacted sales of seasonal items and apparel. Some retailers, however, noted an exceptional pickup in sales of men's apparel. Home-related items (electronics, appliances, furniture, etc.) remained some of retailers' strongest selling items. Despite slower-than-expected sales, inventories were described as being at or slightly below last year's levels, and there were no reports of increased promotional activities. Most retailers, citing unwavering consumer confidence, were very optimistic about the upcoming holiday shopping season. Reports on District light vehicle sales were mixed with some dealers indicating that sales remained strong, while one large District auto group reported that "October (sales) slowed up, hard." This contact also noted that for the first time in a long time they will not be taking manufacturers' full allotment of new vehicles.

Construction/real estate. Overall construction activity slowed modestly as both the residential and business segments showed some signs of softening. Realtors reported that existing home sales had peaked and were decreasing slightly, as buyers became concerned about interest rate increases. A realtor in one of the District's largest metro areas reported that year-to-date sales through September moved roughly even with 1998's results, after running ahead of last year's sales pace through August. One contact reported that in recent months there had been a discernible increase in condominium purchases by investors who planned on either renting the units out or turning them around quickly for a profit. This contact suggested that this was holding down rents on two-bedroom apartments in the market. Growth in commercial construction slowed modestly, but remained robust. One contact noted a slowing in retail development even as vacancies in this segment continued to decrease. Office vacancies also remained very low in most metropolitan areas, but rental rates were not rising as fast as some analysts had expected.

Manufacturing. The auto industry continued to lead the way as overall manufacturing activity remained very strong in September and early October. Automakers expected sales nationwide to remain strong in the fourth quarter, which kept production steady at very high levels in recent months. Inventories were generally lean, notably for some passenger car models. Despite continued strong sales, pricing power remained soft for the auto industry with very little increase in sticker prices and continued heavy use of incentives. The steel industry continued to rebound from 1998's difficulties. The inventory overhang resulting from record imports late last year has been worked down as prices continued to firm and new orders remained strong. Demand for consumer durables, such as small appliances and lawn equipment, was strong although one contact noted a "gentle, gentle" softening in demand for appliances. Production of heavy trucks remained robust, but industry contacts noted that inventories were building and could lead to slower production in the coming months. Demand for construction equipment was reported to be strong, but softening somewhat, and new orders for farm machinery remained very weak. Producers of construction materials reported that new orders remained very strong as these industries continued to run near capacity.

Banking/finance. Overall lending activity remained strong in recent months, although some slowing was noted on the consumer side. Home refinancing activity has dropped off precipitously as mortgage interest rates increased. Refinancing applications at one large money center bank, which earlier in the year accounted for nearly 80 percent of total mortgage applications, fell to 11 percent in recent weeks. At the same time, lenders reported that home equity lines of credit were increasing. One bank noted improved consumer loan quality resulting from the bank's efforts to tighten standards in recent months. On the business side, most contacts indicated that loan volume continued to rise steadily and demand remained strong. One bank noted a pickup in sizable lines of credit to firms with international exposure, who are hedging against Y2K-related problems that may develop abroad. Standards and terms for business loans remained unchanged for the most part, although one bank did report some tightening of standards.

Labor markets. Labor markets remained tighter than the nation as a whole in September and early October amid more frequent reports of intensifying wage pressures and increases in non-wage labor costs. Contacts in industries ranging from casual dining, automobile dealerships, and temporary help agencies reported that wage pressures were intensifying. One staffing service firm indicated that wages were up 10 to 20 percent "across the board since July." This contact reported that the company had to absorb this increased cost for existing orders, but was passing it along to new customers. In addition, a few contacts reported that non-wage labor costs, particularly for health insurance, were rising noticeably. Demand for workers remained strong across industry sectors with the exception of manufacturing, where some pockets of softness continued. A large shipping firm suggested that the dearth of truck drivers, and potential drivers, was leading to softer demand for heavy trucks. Increasing layoffs and upward-trending unemployment rates were reported in a few of the less-diversified, highly industrialized metropolitan areas, especially those highly reliant on farm machinery production.

Agriculture. The fall harvest was moving rapidly throughout the District in mid-October and was well ahead of the average pace thanks to dry weather. The favorable weather also helped lower fall expenses by reducing the amount of natural gas required to dry grain for storage. However, the dry weather also hurt pasture conditions in Indiana and Illinois. Several agricultural bankers reported that yields were better than expected, contributing to tight storage availability in some areas. One grain elevator near Sioux City, Iowa had already placed several thousand bushels of corn on the ground as of mid-October. The *Hogs and Pigs* report released near the end of September confirmed the industry is in a liquidation phase that began three months earlier. District states registered an especially sharp decline in the size of the breeding herd. The number of breeding animals dropped 20 percent in Illinois and Wisconsin, was down 11 percent in both Indiana and Iowa, and declined 8 percent in Michigan. In comparison, states outside the District reported an aggregate decline of 6 percent in the size of the breeding herd. The value of U.S. agricultural exports is projected by the USDA to increase 2 percent during fiscal year (Oct.-Sept.) 2000. However, gains are expected to be marginal for District farmers because an increase in the export value of soybeans, meal, red meats, and dairy products will likely be offset by a decline in the export value of corn and soybean oil.

EIGHTH DISTRICT - ST. LOUIS

Summary

The District economy continues to operate at what appears to be full capacity. Contacts have noted some moderation in growth lately that they attribute partly to ongoing shortages of workers. Examples of upward wage pressures have recently become more frequent. Home sales continue to be strong in most parts of the District, although pockets of weakness are popping up. Commercial real estate markets remain robust. Consumer loan demand is boosting loan growth moderately at banks, although bankers are becoming increasingly concerned about delinquency rates. The fall harvest is ahead of schedule for most crops, although yields are generally below average.

Manufacturing and Other Business Activity

District contacts report that growth has moderated slightly in the past two months, partly because tight labor markets continue to limit production at many firms, especially small ones. Ongoing record low unemployment rates have forced many firms to search for workers outside their local areas. FedEx, for example, reports recruiting hourly workers from outside the Memphis region. Firms also continue to use cash bonuses to attract and retain workers. Concerns about finding a sufficient number of qualified workers have delayed some firms' expansion plans.

Contacts report that upward wage pressures have picked up recently—in some cases, wage increases are approaching 6 percent. Contacts also note that health care costs are rising dramatically, and hikes of 10 to 15 percent are common. Rising pharmaceutical costs are a primary reason.

Strong sales growth has been reported in the plastics and building-materials industries. Computer hardware- and software-support companies are also flourishing, with many high-tech firms moving into, and expanding within, the District. Truck producers continue to enjoy a boom, with year-to-date sales through September topping 1998 totals.

Despite the overall robust economy, several plant closings and downsizings have also been reported. Declining demand for major household appliances has led to ongoing workforce reductions at General Electric. Even though the poultry market has recently rebounded somewhat, poultry prices are still off about 20 percent from a year earlier. Cutbacks in the industry are expected. Because of poor conditions in the agricultural sector, farm equipment dealers have seen demand fall off sharply and inventories rise to unusually high levels.

Real Estate and Construction

Although most residential real estate agents report that home sales around the District remain strong, with many areas continuing to experience growth, some agents have noted a slight weakening. Inventories of available homes have grown recently in several areas, especially Memphis, relieving some of the shortages that had existed for much of this year.

After a moderate decline in July, monthly residential building permits rebounded sharply in August, spurred by strength in the multi-family housing market. Year-to-date residential permits are above their year-earlier levels in almost all District metropolitan areas. Many contractors are still concerned, though, that ongoing shortages of skilled workers and certain materials will continue to delay some projects.

Commercial real estate markets remain strong. However, some commercial real estate agents report that the demand for industrial space is not being met because rental rates in some areas have not yet risen enough to justify new construction.

Banking and Finance

Total loans outstanding at a sample of large District banks grew less than 2 percent between mid-August and mid-October. This growth came entirely from consumer loans. Real estate loans were unchanged, and commercial and industrial loans were down mildly. Recent conversations with contacts at small and mid-sized banks revealed that deposits have picked up recently and that loan demand remains strong, particularly for consumer loans. Many bankers are becoming increasingly concerned about delinquency rates, especially for agricultural loans, and have upped their loan loss reserves accordingly.

Agriculture and Natural Resources

Despite recent rains, fall harvest conditions have generally remained quite favorable throughout the District. For example, the District-wide corn harvest, and the cotton harvest in Arkansas, Mississippi, Missouri and Tennessee are ahead of both last year's paces and their five-year averages. The soybean harvest is also ahead of schedule in all District states except Mississippi.

Persistently dry conditions in August and September, however, have reportedly reduced soybean yields below last year's levels in most District states. Cotton growers are experiencing lower-than-average cotton yields. In addition, they are worried that below-average crop quality will exert downward pressure on revenue. Corn yields in Arkansas, Illinois, Mississippi and Tennessee, on the other hand, are up from a year earlier. Early reports suggest that rice yields will be either average or slightly below average this season. A shortage of subsoil moisture in Illinois may hinder the emergence of the winter wheat crop.

NINTH DISTRICT--MINNEAPOLIS

The overall Ninth District economy remains highly charged, although agriculture's batteries are running low. Construction, consumer spending and manufacturing are energizing the economy. Moreover, the mining and energy industries are recently showing signs of recharging. However, low prices are reducing the power of this fall's bountiful harvest. Meanwhile the tight labor markets are generating wage pressure as several businesses report boosting worker pay. Overall prices remain level but the cost of some items is accelerating.

Construction and Real Estate

"Construction is still going strong," said a North Dakota builder, which describes the current state of construction throughout the district. A Wisconsin bridge-girder manufacturer will expand operations by over 10 percent due to increases in federal funding for bridges over the next five years. A $20 million amphitheater project is planned for a Minneapolis suburb. In Minnesota and the Dakotas, construction contracts awarded rose 3 percent in the three months ending in August from a year earlier. District housing units authorized grew by 3 percent in the three months ending in August from a year earlier.

Consumer Spending and Tourism

Consumer spending is robust. Sales are up 7 to 10 percent compared to a year-earlier at a large Minneapolis area mall, and up 10 percent at a regional mall in Fargo, N.D. Several large retailers are expecting holiday sales to increase 10 to 15 percent over 1998 levels. Auto sales are level with last year in North Dakota. The consumer market for educational games is "very, very strong," reported an advisory council member. However, retail sales are weak in agricultural areas of northeast Montana, according to a bank director.

Fall tourism is steady across most of the region. Northern Wisconsin is on par with a year earlier following a strong close to the summer season. A chamber of commerce representative in northwest Minnesota reports increases in tourism traffic compared to a year earlier. Hotel occupancy and visits to attractions are flat to down slightly in South Dakota compared to year-earlier levels, but tourists are spending more than last year, according to a tourism official. Montana tourism is steady overall, but summer tourism finished down in Glacier National Park and other northern destinations compared to a year earlier.

Manufacturing

Manufacturing in the Ninth District remains robust, with many manufacturers reporting strong sales and expansion plans. A Minnesota home improvement product manufacturer plans to add new equipment and staff to meet rising demand for its products. A Wisconsin plastic products manufacturer reports an increase in both sales and development and is considering building another plant. A North Dakota equipment manufacturer reports year-to-date sales up 5 percent as compared to last year. A Wisconsin industrial products manufacturer is expanding production capacity due to increases in product sales. In addition, an October St. Cloud State University (Minnesota) survey reveals an increase from the previous survey of hours worked at area manufacturing establishments.

Mining and Energy

The metal-based mining industries are starting to rebound as evidenced by increases in iron ore production. Increases in steel plant utilization and reductions in iron ore inventories have spurred some iron ore mines to reopen. A Minnesota iron ore mine production line reopened in September and two Michigan iron ore mines reopened in October. Most mine workers have agreed to a five-year contract, which should reduce the risk of work stoppages.

Meanwhile, oil exploration activity has picked up. In October, 10 rigs were operating in North Dakota, three rigs in South Dakota and four rigs in Montana as compared to four, zero and four, respectively, in July. In addition, August oil production in the district was up 2 percent from June production levels.

Agriculture

Current crop production forecasts for the district suggest a bountiful harvest. Expected soybean, hay and sugarbeet production for Minnesota, the Dakotas and Montana in 1999 is above the hefty 1998 harvest levels. However, expected 1999 corn production in Minnesota and the Dakotas is 10 percent below the record 1998 harvest amounts, and 1999 small grain production in North Dakota is significantly below 1998 levels. Farm income, however, remains depressed as dismal agricultural prices are offsetting the bumper crop.

Employment, Wages and Prices

"There is more stress on finding help than customers," reported a mall manager in North Dakota, a theme heard across the district. A South Dakota state labor official said that employers are "looking for good prospects, and they're hard to find. I don't see anything changing that." Economic development officials in Fargo, N.D., reported that businesses may soon pool resources to offer scholarships or pay off school loans to attract employees. Even though significant layoffs are reported in La Crosse, Wis., employers in the region still cite difficulty in finding labor. A St. Cloud State University survey reveals that 55 percent of survey respondents indicate that it was more difficult to attract qualified workers in September than it was three months earlier.

Wages and salaries are increasing in response to tight labor markets. Some employers in the district are offering starting bonuses for entry-level retail positions. A medical center in La Crosse, Wis., reports a 4 percent hike in wages. Union workers at food plants in southern Minnesota negotiated over a 2 percent raise each year for four years, and a 12 percent increase in starting pay. Montana directors reported wage pressure for middle-management and retail positions, and local unions are bargaining for higher wages. Several Montana industries, however, report steady wages.

Some product prices are increasing; however, the upward pressure on wages isn't spilling over to most prices. An informal survey of manufacturers in Minnesota and Wisconsin indicates that input and product prices are largely holding steady. High productivity and low prices on products coming from abroad are restraining overall price increases. Exceptions include climbing construction-input costs, health insurance costs, milk prices and gas. Health insurance costs are expected to increase 12 percent next year reported an advisory council member. Corrugated paper prices are expected to increase 10 percent next year, reported another advisory council member. Costs for residential heating oil and natural gas are expected to increase this winter.

TENTH DISTRICT - KANSAS CITY

Overview. The district economy slowed further in late September and early October. However, the overall level of activity remained solid, at a level similar to a year ago. Retail sales declined but are expected to pick up heading into the holiday season. Manufacturing activity slowed from a strong August, and the construction sector showed signs of improvement following flat growth during the summer. In the farm economy, the fall harvest is on schedule, but big grain crops could continue to hold down crop prices. Labor markets in most of the district remained very tight, and reports of wage pressures were slightly higher than in recent surveys. Retail prices edged down, while prices for some construction and manufacturing materials continued to rise.

Retail Sales. Retailers in the district reported a decline in sales, following flat activity in the three previous surveys. Sales of men's business wear were particularly weak, while appliances sold well. Inventory levels continued to expand and are expected to rise further, as stores gear up for the holiday season. Motor vehicle sales remained strong in most parts of the district, particularly for trucks and SUVs. Expectations for future vehicle sales weakened from earlier in the year. Vehicle availability was only a concern for some models of light trucks.

Manufacturing. District factory activity slowed after making some progress in August. While most plants were still operating at medium to high capacity, fewer contacts than in the previous survey reported high levels of capacity utilization. Manufacturing materials remained generally available, but lead times increased for steel and some other metals. Concerns about future material availability remained low. Managers were much more satisfied with inventories, and most plan to continue trimming stock levels in coming months.

Housing. Building activity improved following several months of decline, but was flat compared with a year ago. Builders expect a typical seasonal downturn in activity heading into the winter months. Material availability problems eased somewhat from previous surveys, but gypsum board and insulation remained scarce in some areas. Home sales declined, and inventories of unsold homes built up in some rural areas. Mortgage demand continued to fall as refinancing activity has slowed substantially with rises in interest rates.

Banking. Bankers report that loans increased and deposits held steady last month, raising loan-deposit ratios. Demand increased for commercial and industrial loans, commercial real estate loans, and consumer loans. Demand for home mortgage loans fell. On the deposit side, increases in demand deposits and MMDAs were offset by a decline in large time deposits. A few respondent banks raised their prime lending rates and consumer lending rates last month, but most banks held rates steady. Almost half the banks expect to increase their prime rate and consumer lending rates in the near future. Lending standards were unchanged.

Energy. District energy activity continued to improve, as energy prices remained high. The rig count in mid-October was nearly as high as a year ago and 60 percent above the March low, as both oil and gas prices remained well above year-ago levels.

Agriculture. The district's fall harvest is on schedule. Corn and soybean yields in much of the district are better than normal, but cotton yields are well below normal due to dry weather. The big grain crops promise to hold crop prices down in the months ahead. The lower prices, however, have trimmed feed costs and boosted profits for cattle feeders. Despite the bigger profits, cattle ranchers have not begun to enlarge their herds as expected. Low hog prices have forced many of the district's small-scale hog producers out of business, and many remaining producers operate under contractual arrangements with food companies. District bankers report farm loan portfolios are generally stable, but repayment of farm loans may slow unless farm incomes improve. The bankers also report slower business activity in many farm dependent rural communities.

Wages and Prices. The district's weaker economic activity in recent months has not eased labor markets much, since labor force growth in the region has also slowed substantially. Most contacts continued to report difficulties filling positions. Some manufacturers noted an increase in the availability of production workers, but retailers and builders reported continued difficulties in finding sales associates and skilled tradesmen. The number of contacts reporting increased wage pressures was up slightly from the three previous surveys. Retail prices edged down but are expected to inch up as the holidays approach. Prices for some manufacturing materials continued to increase and are expected to rise further in coming months. Prices for construction materials also continued to rise, although not as quickly as in the last six months.

ELEVENTH DISTRICT--DALLAS

In September and early October, Eleventh District economic activity expanded at about the same pace as reported in the last beige book. Manufacturing activity accelerated slightly, and demand for oil services continued to increase at a slower pace than drilling activity. Demand for services was steady and strong, while credit conditions, deposit growth and demand for loans were stable. Retailers reported that sales growth was slightly slower but still strong. Construction activity was slightly slower, and drought caused increasing problems for agricultural producers.

Prices. Prices of labor, services and a few goods rose, but most other prices were steady or down. Contacts across many industries reported difficulty finding and keeping workers. Retailers reported that entry-level turnover was 200 to 300 percent a year. A trucking firm reported that some trucks are standing idle because labor is so scarce. As a result, wages rose in many service industries, such as retail and auto sales, business services and trucking and air transportation. However, only a couple of goods-producers increased wages (by 5 to 20 percent.) Prices of memory chips rose 25 percent from a few months ago. Petrochemical prices increased, but contacts expected a decline in coming months with increases in production capacity. Aluminum prices rose 2 to 3 percent, and business service contacts encountered less resistance to fee increases. Prices of clay, fabricated metal, apparel, paper and food products, office space and transportation services were steady. Prices of oil, gasoline and natural gas fluctuated over the past six weeks, but returned to about the same levels as reported in the last beige book. Retail prices were slightly lower, and telecommunications equipment and services prices continued to fall. Prices of lumber and wood products fell 4 to 5 percent over the past three months, and timber prices also fell seasonally. Cement prices fell by as much as 12 percent in some locations.

Manufacturing. Manufacturing activity accelerated slightly in the past six weeks. Semiconductor sales growth picked up slightly, in part due to increased sales of wireless phones and the usage of more chips in each phone. Contacts reported that memory chip production from

Taiwan was back on line following the September earthquake, but users of memory chips have increased their inventories in case of further supply disruptions. Sales of food products, finishing woods and apparel rose. Sales of some petrochemicals rose with improved demand in Asia. Demand for timber and lumber was steady, but stronger than last year, in which firms saw declines associated with the Asia crisis. Sales of primary and fabricated metals, boxes and packaging materials were unchanged. Sales of concrete declined in a couple of areas but were stable elsewhere, and contacts reported that cement inventories were too big. Sales of clay products were steady, with the exception of brick sales, which weakened due to softer home sales and backlogs in brick production.

Services. Demand for services was steady and strong since the last beige book. Temporary services contacts reported continued increases in demand for temporary workers for the energy sector, continued strong demand for workers with high-tech skills and steady demand for manufacturing workers following an increase in the summer months. However, growth in customer service and IT-related jobs slowed as Y2K-preparation work was completed. Legal and accounting contacts reported strong and steady activity, boosted by transactions, utility deregulation and construction of government and school buildings. However, trial work has been depressed recently. Railroad cargo volumes were up over the past month, and trucking activity was steady and strong but weaker compared to early this year. Passenger airlines reported that while earnings were hurt by the hurricanes, demand remained strong.

Retail Sales. Retailers reported weaker sales growth in the first half of October than in September. Several retailers said that, despite this softening, sales were still strong. While no inventory problems were reported, a few said that October sales were below projections and one contact worried that inventories might swell if sales growth continued to decelerate. Contacts said they expect good sales growth through Christmas. Auto sales remained at very high levels.

Financial Services. Credit conditions, deposit growth and demand for loans were stable over the past six weeks. While higher interest rates dampened lending growth, contacts reported that auto, real estate and home equity lending remained at high levels. A contact in the securitization industry said some major financing companies will cut office financing from November through January because of their expectations that Y2K-related uncertainty could cause interest-rate gyrations which they want to avoid.

Construction and Real Estate. Construction activity was slightly slower in recent months, with fewer commercial projects being started. In some areas, builders reported that shortages of labor and materials, and backlogs of unbuilt homes had subsided somewhat. New home sales slowed but remained strong over the past few months, as higher mortgage rates dampened demand. Contacts reported that this softening in home sales may have boosted absorption of multifamily units. However, completions of new apartments are expected to outpace demand over the next year, leading to a slight decline in occupancy rates. New office construction has outpaced absorption in Houston and Dallas, lowering occupancy rates a bit.

Energy. The domestic rig count rose 7.5 percent over the past six weeks, but the increase in demand for oil services was not as great, as the new drilling remained onshore, shallow and gas-directed. Offshore and international oil services work continued to decline slightly. This lack of response to higher oil prices was attributed to several factors: expectations that price gains were temporary, mergers that drew resources away from other investment, and the inability of some independents to obtain financing after they violated their loan covenants during the most recent period of low oil prices.

Agriculture. Drought is a growing problem for agricultural producers. Harvesting continued, but land preparation slowed due to a lack of moisture. Most pastures had limited forage for livestock, and supplemental feeding and herd reduction continued in most areas.

TWELFTH DISTRICT — SAN FRANCISCO

Summary

Reports from contacts indicate continued strong performance from the Twelfth District economy in recent weeks. Sales of retail merchandise and services reportedly were rapid in most District states during the recent survey period and respondents noted a pickup in District manufacturing activity. Conditions among District agricultural producers were mixed, as prices improved for ranchers but remained poor for farmers. Conditions in District real estate markets were strong overall, although slower home sales tempered growth in construction in some states. District financial conditions remained healthy, and competition for quality borrowers continued to be intense. Throughout the District, respondents reported difficulty finding and keeping qualified entry-level and skilled workers.

Business Sentiment

District respondents expect continued strong performance in the national economy and their respective regional economies during the next four quarters. Most respondents expect national GDP growth to return to its long-run average pace, leaving the national rate of unemployment at or near its current level. Still, an increasing number of respondents expect inflation to edge up in coming quarters. Although one-half of District respondents still expect economic growth in their region to outpace growth in the national economy over the next year, a growing number of respondents expect growth in their region to slow to the national pace. Most respondents anticipate little change in the strength of business investment and consumer spending in their areas. In contrast, nearly two-thirds of District respondents expect housing starts to slow in coming months, a larger share than in the previous survey.

Retail Trade and Services

Sales of retail merchandise reportedly were rapid in most District states during the recent survey period. Respondents noted robust sales of food, pharmaceuticals, home furnishings, home electronics, and appliances. In contrast, sales of apparel slowed in recent weeks, as unseasonably warm weather damped shoppers' appetites for fall and winter fashions. Retailers commented that inventory levels were generally sufficient, with few problems obtaining merchandise from suppliers. However, respondents noted that wholesale prices are rising on several types of products, most notably food and pharmaceuticals. Conditions among District service providers remained strong in recent weeks. Respondents reported robust demand for telecommunications, Internet-related services, and cable television services. Demand for shipping and freight services increased in many District states, as exports to East Asia continued to improve. In contrast, growth in tourism slowed in Utah and Southern California, boosting hotel vacancy rates in those areas.

Throughout the District, respondents mentioned difficulty finding both entry-level and skilled retail trade and service employees. Moreover, training times and employee turnover are increasing. Respondents noted that many firms are paying existing employees commissions for finding new hires and that signing bonuses, stock options, and year-end bonuses are now a must in hiring skilled information technology workers.

Manufacturing

Manufacturing contacts throughout the District experienced solid gains, as expansions in petrochemical production, paper processing, and steel manufacturing augmented ongoing growth in high-technology equipment manufacturing. Rapid growth in demand for year-end publications and business and government forms apparently has increased orders for paper products in recent weeks, raising prices and producing occasional shortages of materials, such as titanium dioxide, the primary whitening pigment for paper. Respondents reported that orders for domestic steel products rose in recent weeks. Demand for telecommunications and computer equipment remained strong and respondents noted that order backlogs are growing. Respondents pointed out that supplies of several key inputs to high-tech manufacturing, most notably memory chips, were interrupted by the recent earthquakes in Taiwan. Decreased supply has boosted chip prices, but according to respondents, higher input prices have not been passed on to final sales prices.

Agriculture and Resource-related Industries

District agricultural producers reported mixed conditions during the most recent survey period. Conditions for cattle ranchers continued to improve in recent weeks. Beef producers have benefitted from strong sales, increased prices, and stable costs. Conditions also have been favorable for District dairy, stone fruit, citrus, avocado, and rice producers. In contrast, low commodity prices and poor growing conditions continue to affect wheat, cotton, sugar beat, and vegetable growers. Respondents throughout the District reported significant difficulties obtaining seasonal agricultural workers.

Real Estate and Construction

Real estate construction and sales activity remained at high levels in most District states, although the pace of growth reportedly slowed, particularly for residential properties. Contacts in many District states noted that home sales have slowed and sales price appreciation has decelerated from earlier in the year, tempering growth in new residential construction. The notable exceptions to the slowdown in residential markets are the San Francisco Bay Area and Phoenix, Arizona. A number of contacts noted that a slowing rise in residential rental rates, both of apartments and homes, has begun to affect speculative building in that market. Commercial real estate markets remained solid in most District states, although building permit activity reportedly is down from last year. Building materials and skilled construction workers remain in short supply throughout the District. However, respondents noted that in most cases material and worker shortages are being translated into longer completion times rather than higher prices and wage rates.

Financial Institutions

District financial institutions continued to report healthy loan demand and generally good credit conditions. Financing remains readily available for qualified businesses and stiff competition is encouraging lenders to offer more favorable financing terms. Comments from respondents point to continued solid credit quality, although there were scattered concerns about the health of highly leveraged businesses. Throughout the financial industry, shortages of qualified workers continued to be a primary concern, and wage and salary pressures remained high.