For use at 2:00 p.m., E.D.T.
Wednesday
August 6, 1997

Summary of Commentary on ______________________

Current Economic Conditions

by Federal Reserve District

July 1997

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS BY FEDERAL RESERVE DISTRICTS

JULY 1997

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SUMMARY[1]

Overview: Economic activity generally expanded at a moderate rate in many districts in June and July, although several reported that growth was more brisk. The tempo of consumer spending picked up since the last Beige Book report, aided in part by improved weather. Automobile sales, however, were slightly softer. Manufacturing remained at a high level or expanded further across most industries, particularly for nonautomotive durables. Most districts indicated that manufacturers' inventories remained at generally desirable levels. Commercial real estate activity strengthened across much of the country as vacancy rates declined further and rents rose. Home sales and construction increased modestly in recent weeks, but still lagged slightly below year-ago levels. Labor markets tightened further but only scattered wage pressures were noted. Prices for most goods were stable, although reports indicated that lumber and some agricultural prices rose. Recent rains in some districts brought relief to crops damaged by heat and sparse rainfall. Several districts indicated that commercial lending strengthened while reports on consumer lending were more mixed.

Consumer Spending: Most districts reported stronger retail sales since the last report; only Kansas City had weaker activity. July's sales were noticeably stronger in New York, Richmond, and Minneapolis, with descriptions of sales ranging from "well above plan" to "vigorous." Philadelphia, Atlanta, and San Francisco, however, reported more modest

[1]Prepared at the Federal Reserve Bank of Richmond and based on information collected before July 28, 1997. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

improvements. Dallas indicated that consumer expenditures were mixed across that district.

Some districts attributed a rebound in sales growth to the arrival of warmer weather. However, New York stated that increased sales were not limited to seasonal items. Minneapolis reported that sales had increased, in part because some consumers had to replace flood-damaged belongings. Apparel demand appeared stronger in many districts, with Boston, New York, and Chicago citing particular strength in sales of women's fashions. However, Cleveland characterized the demand for children's apparel as soft, and Boston had weak sales of men's clothing. Consumer purchases of big-ticket items increased in New York, Richmond, and Chicago. Chicago also noted that sales of some luxury items were up "noticeably" from a year ago, particularly of personal watercraft and all-terrain vehicles. In most districts, vehicle sales edged lower; sales of light trucks and sport utility vehicles continued to display considerable strength, but sales of domestic passenger cars softened.

Retail inventories were in line with sales across most districts. New York, Philadelphia, Cleveland, Atlanta, and Chicago reported that retailers' inventories were on target. Kansas City said that retailers there had trimmed inventories and did not believe further reductions were necessary.

Tourism: Tourism continued to strengthen in much of the country. Hotel occupancy rates were generally described as very high. Atlanta noted that the luxury hotel segment continued to post strong growth, and that hotels in Florida enjoyed high occupancy rates despite not offering normal off-season discounts. Philadelphia noted increased business travel and a greater number of summer vacationers. Minneapolis, however, indicated that visits to national parks were "on the soft side," while San Francisco said that vacation traffic was weak in Hawaii but normal elsewhere.

Manufacturing: Many districts reported that there was further expansion in manufacturing activity. Production picked up in the Boston, Philadelphia, Cleveland, Chicago, and Dallas districts, and continued at moderately high levels in the Richmond, Kansas City, and San Francisco districts. New York reported moderate growth in manufacturing, while Minneapolis noted that growth there was "solid, but not spectacular." Atlanta described growth as mixed.

Production rose for aircraft and related products in the Boston district, but a shortage of skilled labor slowed aircraft production in the San Francisco district. Atlanta noted strength in shipbuilding. Chicago indicated that steel producers and manufacturers of heavy equipment continued to see increased production and strong orders. In the Cleveland district, however, demand for steel moderated, and in Philadelphia's district, primary metal producers faced slackening demand. Weaker demand for textiles reduced production in the Richmond and Philadelphia districts, while continued softness in apparel demand forced further plant closings in the Atlanta district. Furniture manufacturers in the Richmond district reported weaker product demand. The Philadelphia and Dallas districts noted greater demand for construction and building products.

Few inventory problems were noted. Philadelphia and Kansas City reported that stocks of manufactured goods had been trimmed slightly, and further reductions were anticipated by Kansas City. Inventories in the Cleveland district were only slightly higher than earlier in the year.

Construction and Real Estate: Residential real estate activity was reported to be higher in some districts, but mixed in others. Chicago noted an increase in sales of existing homes in June, but indicated that year-to-date sales continued to lag. Contacts in the Dallas district reported increases in home sales and housing construction, particularly for more affordable homes. Housing starts edged lower in the Kansas City district and were generally unchanged from a year ago. Reports on residential permits were mixed; St. Louis and New York noted increases while Chicago reported that building permits were below those of a year ago.

Most districts reported strong commercial real estate activity, with declining vacancy rates and vigorous construction. Several districts also reported rising rents, from "modestly" in New York, to "sharply" in Boston. Richmond, St. Louis, and San Francisco reported strong nonresidential construction activity, as did Atlanta, although a lack of suitable land there was slowing industrial development. In the Chicago district, some areas experienced "record levels of activity," and Cleveland reported that "commercial building improved from the spring."

Labor Markets: Labor markets strengthened during June and July. Boston, Cleveland, Richmond, Atlanta, Chicago, St. Louis, and San Francisco reported tight labor markets and shortages of skilled workers. Most manufacturers in the Boston district described the pool of available labor as adequate, but Chicago and San Francisco indicated that labor shortages had curbed production in those districts. Finding employees with adequate computer skills prompted some employment agencies in the Cleveland and Richmond districts to offer in-house training. Employees for entry-level and retail positions were increasingly difficult to find and retain in the Cleveland, Chicago, St. Louis, and Kansas City districts.

Despite the persistent labor market tightness, wage pressures remained generally subdued. Exceptions included Richmond, where retail wages surged in July, and Chicago and Kansas City, with intensifying wage pressures for low-paying, entry-level, and clerical positions. Minneapolis described increased wage pressures accompanied by higher benefits costs. In the Boston district, employers were enhancing compensation packages and offering up-front bonuses to attract job candidates. Dallas reported that more employers were offering nonpecuniary forms of compensation instead of raising wages.

Prices: Overall prices were stable, and contacts in many areas attributed their inability to raise prices to competitive pressures. Boston, New York, Philadelphia, Atlanta, Chicago, and Kansas City generally reported that prices remained steady; Cleveland saw only modest increases. Minneapolis noted that product prices for intermediate and final goods remained "quiescent." Several districts did refer to price movements in agriculture and energy. Minneapolis reported higher hay, cattle, and hog prices, and Dallas noted that lumber prices were up. Minneapolis, Kansas City, and Dallas indicated that gasoline and crude oil prices were falling, and Kansas City noted lower wheat and fed cattle prices as well. San Francisco reported downward price pressure on meat and produce in grocery stores, although cattle prices there had "firmed further."

Agriculture and Natural Resources: Generally, crop conditions appeared to be in good shape, although warm, dry weather hampered crop development in several districts. Cleveland, Richmond, Chicago, St. Louis, and San Francisco reported that below normal rainfall caused some deterioration in crops. Recent rains, however, brought relief to farmers in the Richmond and Chicago districts. Chicago noted that the rains came at a critical time for pollination, and

Richmond suggested that while it may be too late for some crops, the rains would prove beneficial on balance. Elsewhere, dry weather helped crop development in Texas and promoted fruit and nut yields in California.

Livestock remained in good condition, and beef and hog producers enjoyed higher prices. Kansas City reported that many producers were marketing cattle early to head off further price declines, and that hog producers were expanding their operations. In Minneapolis, output from beef and hog producers was steady.

Energy activity continued to improve, with Minneapolis stating that, because of new rigs coming on line, oil and gas exploration in that district was at its highest level in more than a decade. Kansas City reported that the rig count was well above a year ago, while Dallas noted that the rig count there had leveled off.

San Francisco indicated that logging operations continued to expand at a "good clip." In sharp contrast, Minneapolis reported a noticeable decrease in Montana's production of forest products. Iron and steel production in that district also showed signs of falling off, but this was attributed to structural changes rather than weaker demand.

Banking and Finance: Overall lending activity was mixed across districts. Commercial lending increased in several areas of the country. Cleveland, Richmond, Atlanta, and Chicago reported that commercial loan demand remained strong. Consumer lending was higher in Philadelphia and Cleveland, flat in Chicago, and down in the St. Louis district. Both Philadelphia and Chicago noted some increases in home equity lending. Residential mortgage demand was described as higher in the Richmond district, stable in the New York district, and relatively flat in the Atlanta district.

Delinquency rates fell somewhat in several districts. New York and Philadelphia reported that delinquency rates continued to decline for most types of loans. Delinquencies remained low in the Dallas district, especially in consumer lending. However, Cleveland reported a slight increase in consumer delinquencies. Cleveland and Kansas City reported tightening of credit standards, as some bankers cited concerns over credit quality.

FIRST DISTRICT - BOSTON

The First District economy continues to expand at a moderate pace. Most retail and manufacturing contacts report rising revenues and little change in prices. Employment is steady or up slightly, and wages are generally said to be rising at a 2 to 6 percent annual pace; the exceptions are specific occupations in short supply, mostly technical and highly skilled jobs, which command greater wage increases plus other rewards. Commercial real estate continues to improve in New England, with the Boston market very strong. Insurance companies' revenues are rising, but they are cutting employment.

Retail

Most retail contacts report that sales are increasing at a steady, moderate pace. Sales gains in the second quarter are said to be in line with expectations. Some inventory buildup occurred, largely because of weather-related slowness in April and May, but sales growth has since rebounded to its pre-April pace. Reported areas of strength include women's and high-end apparel, building materials, office supplies, and tourism, all of which reported mid to upper single-digit growth rates. Areas of weakness, with modest sales declines, include hardware and men's apparel. Appliance sales have been weak throughout the year, but office and home computers are said to be rebounding from earlier depressed levels. An additional area of weakness is the discount retail sector, which is undergoing significant consolidation with many bankruptcies and store closings recently reported.

Employment is reported to be either steady or increasing in line with sales. Contacts mention pockets of labor market tightness, including jobs in construction, tourism, and highly skilled occupations. Low-skill workers still appear to be abundant. Wages are reported to be growing at a 4 to 6 percent pace.

All respondents report that competitive pressures are keeping both their suppliers' and their own prices steady. Profit margins are also holding steady. Across the board, contacts say that efficiency improvements (better inventory control, automation, and purchasing efficiencies) are required to maintain profitability. Most respondents have moderated their capital expansion plans, but tourism and office supply firms are expanding rapidly.

Looking forward, retailers expect steady growth with low inflation continuing through 1997. While contacts evince nervousness that the good times can't last forever, they express cautious optimism about 1998.

Manufacturing

Revenue results vary widely among the First District manufacturers contacted. One-third report double-digit percentage increases from a year ago, another one-third report single-digit increases, and the remaining one-third report flat or declining business. Aircraft-related, biotech, and non-automotive consumer durables products are showing the most rapid growth. Results for automotive suppliers are highly variable because production trends differ across vehicle makes and because of extensive realignments of purchasing relationships.

Most manufacturers indicate little if any pressure from materials costs, although furniture-grade lumber and copper costs are said to be rising. Selling prices are also largely stable. Contacts across a wide spectrum of industries mention that large firms are using their market power to contain costs.

A majority of respondents report that their overall employment is unchanged or up a little from a year ago. Several mention difficulties filling openings in information and health technologies, engineering, and skilled blue-collar occupations; in most cases, improved compensation packages or up-front bonuses are necessary to attract candidates. More generally, however, manufacturers tend to describe labor availability as adequate and appear satisfied with paying wage and salary increases in the range of 2 to 4 percent. In addition, one-quarter indicate they are expanding their use of variable, performance-based compensation.

About one-half of the manufacturing contacts report making heavy capital investments this year. These projects include additions to capacity (in some cases, to introduce new products) and expenditures on management information systems. Most other respondents say that capital spending levels remain normal.

Several manufacturers express satisfaction with prospects for continued macroeconomic growth and low inflation, although others mention the challenges of operating in a highly competitive environment or the risks of further appreciation of the dollar. Several contacts are focused on particular industry trends such as improving demand in computer-related markets or prospective declines in automotive-related business.

Commercial Real Estate

Commercial real estate markets in New England continue to improve. The Greater Boston area, driven by rapid growth in financial services and software, is extremely strong. Vacancy rates have reached historic lows, pushing rents up sharply for scarce office and industrial space. There are signs of new office development in the suburbs and talk of two projects downtown, although it will be some time before any substantial increase in inventory materializes. Conditions in the rest of New England are improving, for the most part. Much of Connecticut continues a slow recovery, although downtown Hartford still has substantial unoccupied office space. Maine has shown improvement and modest price increases are reported in Portland, Camden, and Bangor, but Aroostook county is still doing poorly. Rhode Island continues its recovery, especially in the industrial sector, where new buildings are under consideration. Several contacts express concern about the retail market, which had been improving but is now girding for major bankruptcies that will free up several million square feet of space across New England.

Nonbank Financial Services

Respondents at insurance companies report revenue increases in the range of 5 to 20 percent in the second quarter compared to a year earlier. Growth was highest in health care and in investment products with returns tied to the stock market, such as variable life insurance, variable annuities, and mutual funds. Employment was down at the majority of respondents and this trend is expected to continue. Respondents note wage pressures in selected occupations, particularly in technology and investment management.

SECOND DISTRICT--NEW YORK

The Second District's economy expanded at a somewhat faster rate than in the last report, led by a rebound in consumer spending. Retail sales, which had been held down by unseasonably cool weather for most of the second quarter, picked up in late June and were ahead of plan in July. Office markets throughout the New York metropolitan area continued to tighten in the second quarter, though rents in most areas have risen only modestly. Housing markets continued a trend of gradual improvement in New Jersey and downstate New York but remained depressed in upstate New York. Regional purchasing managers' reports indicate moderate growth in manufacturing activity in June. Price pressures in the District remained subdued. Finally, local banks report some softening in demand for consumer and non-residential mortgage loans, along with a further decline in delinquency rates.

Consumer Spending

Most major retailers in the region report that sales were on or above plan in June and well above plan in the first half of July. Compared to a year ago, same-store sales gains for June and early July ranged from 2 to 7 percent. Sales of seasonal merchandise (air conditioners, summer clothing, lawn & garden, etc.) picked up noticeably starting in mid-June and continuing into July; this was attributed to the later than usual arrival of hot weather and represented purchases deferred from springtime. Some contacts, though, noted that sales improved across the board, and not just in seasonal categories. In most cases, women's apparel continued to be the strongest segment; a couple of contacts report that sales of home furnishings improved in recent weeks and were ahead of plan.

Virtually all of the retailers surveyed report that inventories are in "great shape" thanks to the recent pickup in sales of summer-related merchandise. All contacts reported that merchandise costs are essentially flat, and that selling prices are flat to declining. Retail wage pressures remain subdued, although one contact reports that labor costs have begun rising—mostly for new hires.

Construction & Real Estate

The region's housing market has not changed much since the last report. Prices of Manhattan co-ops and condos, which had surged in March and April, held steady at higher levels in May—up 25 percent from a year ago. New apartment construction in New York City and northern suburbs continued to expand in June—for the first half of 1997, twice as many units were authorized by building permits as a year earlier. Recent changes to New York State's rent-stabilization regulations were relatively modest and should have little impact on average rents in the short run.

Sales and prices of existing single-family homes are up moderately from a year ago in downstate New York and New Jersey, but are down across most of upstate New York. Similarly, permits to build single-family homes have been trending up in the New York City area and are near an 8-year high; however, in upstate New York, permits are down more than 15 percent from a year ago and at their lowest level since the 1981-82 recession. Builders in northern New Jersey report that sales of new homes were "okay but not great" in June and early July. While selling prices are flat, a major concern among builders is high and escalating land costs, reflecting a dearth of usable land.

Commercial real estate markets across the New York City metropolitan area continued to tighten in the second quarter. Midtown Manhattan's office availability was 11.3% at the end of June, down from 11.5% a month earlier; Downtown's rate declined to 21.0% from 21.2%. Both rates fell by a full point during the second quarter. Similarly, vacancy rates continued to trend down in northern New Jersey, Long Island, Fairfield, and Westchester Counties in the second quarter. However, average rents were up only modestly in most areas, except in northern New Jersey, where they have accelerated steadily over the past four quarters and are up 7.5 percent from a year ago.

Other Business Activity

Regional purchasing managers report mixed but generally favorable conditions in the region's manufacturing sector in June, along with negligible price pressures. Buffalo purchasing managers report that new orders and production activity continued to expand, though at a considerably slower pace than in May; purchasers also reported a pause in job growth and stable commodity prices. Similarly, Rochester purchasing managers grew less upbeat about general business conditions in June (though positive responses continued to outnumber negatives), but they also noted strength in the local labor market and an abatement of commodity price pressures. Finally, New York City area purchasing managers report sharp improvement in business conditions in both the manufacturing and non-manufacturing sectors in June, accompanied by a slight pickup in price pressures.

New York City implemented two new transit-fare changes on July 4th that reduced commuting costs for some residents: free electronic transfers between bus and subway (ending "two-fare zones"), and elimination of the 50-cent Staten Island Ferry fare.

Financial Developments

In the latest survey of small and medium sized banks in the Second District, senior loan officers reported stable demand for residential mortgage and commercial and industrial loans over the past two months, but softening demand for consumer and non-residential mortgage loans. Refinancing activity was unchanged. Willingness to lend increased on net, with 19 percent of bankers reporting that they were more willing to lend and none reporting they were less willing. Credit standards remained stable.

Interest rates decreased for all categories of loans, with 36 percent of banks surveyed reporting lower rates. This decrease was especially evident in residential mortgages, with 50 percent of banks lowering rates. Average deposit rates increased, with over 36 percent of banks reporting higher rates.

Delinquency rates continued to decline for all types of loans except residential mortgages, for which delinquencies remained stable.

THIRD DISTRICT - PHILADELPHIA

Economic conditions in the Third District improved moderately in June, and the pickup was continuing into July, according to business contacts around the region. Manufacturers generally reported gains in shipments and orders in July. Retailers noted some growth in sales during June and the first weeks of July, although auto dealers said overall sales of new vehicles were off. Slackening demand for cars offset increased sales of light trucks. Bankers said consumer lending continued to advance and there have been some small increases in commercial lending recently. Tourism officials throughout the District said the summer season was off to a good start, with generally strong attendance at beach and mountain resorts and high hotel occupancy rates in major cities.

MANUFACTURING

Manufacturing activity in the Third District generally continued to expand in July. Nearly half of the industrial firms contacted indicated that orders for and shipments of their products were increasing. Fewer than one in five reported declining demand for the goods they make. The strongest sectors appeared to be fabricated metal products--especially building products--processed food, and stone, clay and glass products. Conversely, some producers of textiles, primary metals, and paper products noted recent slackening in demand and output.

For the region's manufacturing industries as a whole, order backlogs were edging up, but delivery times were unchanged. Inventories have been reduced slightly. There has also been a small increase in employment. Several manufacturers reported that they have been keeping the prices of their products steady in response to continuing strong foreign competition, and makers of consumer goods said retailers have been pressing them to keep prices from rising as they face heavy store-versus-store rivalry.

RETAIL

Retailers in the Third District reported marginal improvements for late June and early July. Jewelry stores posted better-than-average gains; sales of clothing items such as shoes and seasonal apparel also increased, but electronics continued to struggle. Business at consumer services firms was said to be strong, especially for computer-related services. In general, stores did not appear to be overstocked, and there has been little unplanned discounting. Store executives described consumer confidence as strong. Most retailers expect sales to grow consistently for the remainder of the year, and they forecast an increase of around 5 percent, in current dollars, for 1997 as a whole.

Most automobile dealers reported that total sales for June and early July continued on a slight downward trend. Dealers estimate the decline at around 2 percent from a year ago. The light truck market continued to expand at a rate of about 5 percent, year-over-year, but this increase was not enough to offset the declining car market. On average, dealers reported that inventories were generally high, which they said encouraged manufacturers to offer relatively large sales incentives. In contrast to the weakness in new car demand, dealers said sales of used cars remained strong and service activity was high.

FINANCE

Loan volumes were moving up modestly in July, according to lending officers at major Third District banks. Some reported recent gains in commercial lending, especially to small and mid-size companies, but the overall increase in business lending was described as slight. Somewhat larger increases were generally reported for consumer lending, including credit cards and auto leasing. Some banks have stepped up marketing efforts for home equity loans recently, and they have seen an increase in this type of lending. Although bankers noted a recent slowing in the rate of credit card delinquencies, they believe some further deterioration in the quality of credit card portfolios can be expected.

Looking ahead, bankers do not foresee an acceleration of loan growth. Despite the small recent increase in business lending, most of the bankers contacted for this report said the demand for commercial loans is not strong. Consumer lending is expected to continue growing, but only a modest increase is anticipated. Facing declining net interest margins and slow growth in lending, banks in the Third District are increasingly looking to introduce and expand fee-earning financial services for both businesses and individuals.

TRAVEL AND TOURISM

Travel and tourism officials in Pennsylvania, New Jersey, and Delaware gave good reports for the beginning of the summer season. Visitation at beach resorts in New Jersey and Delaware was high on the Memorial Day and July Fourth holiday weekends. Visitor counts at Pennsylvania mountain resorts were also good for those weekends. Campground usage has been very high in many areas of the District, as vacationers have taken advantage of an extended period of warm, dry weather. Hotel occupancy has been characterized as very good in the larger towns and cities throughout the three states. Tourism officials said travel to cities has been higher than usual so far this season because of increased business travel and an increase in the number of vacationers going to cities to visit historic sites and attend cultural events. If current trends continue, tourism officials expect that vacation-related business this summer will exceed last year's in most areas and set records in some places.

FOURTH DISTRICT - CLEVELAND

General Business Conditions

Business activity in the District is expanding amid extremely low levels of joblessness and modest wage and price increases. A growing number of counties scattered around Ohio and northern Kentucky report unemployment rates under 3 ½%. In eastern Pennsylvania, where unemployment is somewhat higher than elsewhere in the District, labor markets are strengthening.

Demand for temporary workers continues to rise, but at a more moderate pace than earlier in the year. Temporary employment agencies are having difficulty attracting and retaining a variety of workers, including experienced secretaries and personnel with computer skills. Many firms are addressing the shortfall of skilled workers through internal training programs. No respondents reported accelerated wage growth.

Construction activity is vigorous, with housing, commercial, and road and highway building all improved from the spring. A shortage of bricklayers is noted.

Manufacturing

District manufacturers report favorable business activity. New orders in the steel industry have moderated since the previous District report, and imports have made inroads into the domestic market. Still, the industry's production is at a good level and inventories are only slightly higher than earlier in the year. Capital goods makers report similar trends, as a recent leveling off in orders has occurred at a very high level of production. The heavy truck industry is operating near capacity, with a backlog that extends through the end of the year. A UAW work stoppage at a major Michigan auto facility did not affect any of the Fourth District's major auto plants.

No significant price increases or materials shortages were observed, but several firms indicated difficulty hiring engineers, and employment agencies reported trouble finding workers for light industrial jobs and filling skilled positions such as welders.

Retailing

A cool, wet spring dampened retail sales, but consumer spending recovered in June, with many District retailers posting year-to-year gains of about 5%. Area retailers expect that, for the year as a whole, receipts will be modestly improved from 1996. Some seasonal softness is noted for children's apparel, which is anticipated to pick up as the school year approaches. Retailers report strength in shoe sales. District contacts are satisfied with inventory levels and say that price increases by suppliers have been light.

Auto dealers report that sales have slowed from the exceptional pace of the previous two years, and imports have recently begun to outperform domestic brands. Dealers, who indicate that competition has reduced prices and increased promotional costs on a wide variety of models, see profit margins narrowing.

New car inventories are said to be "cautiously lean," with the usual shortages of a few popular models. Used car sales remain weak, however, and a few dealers indicated deep price discounts on used vehicles.

Agriculture

District agricultural conditions vary substantially by region and commodity. Crops in central Ohio appear to be only a week behind schedule, and good harvests are anticipated for corn and soybeans. However, the wet spring and dry summer have hampered development of Kentucky's tobacco crop. As of mid-July, only 21% of the crop was rated as good to excellent, while 43% was fair. Moreover, hot, dry weather has caused 77% of Pennsylvania's corn to be rated as very poor to fair, and farmers in that region report that the corn fields are much in need of moisture as they enter the critical pollination period.

Spring flooding affected strawberry farmers in southern Ohio and northern Kentucky, and an estimated one-third of the crop has been lost. Cold weather this spring has adversely affected the District's tree fruit industry.

Banking and Finance

Commercial loan demand remains strong, with only a few banks reporting otherwise. Consumer loans and mortgage refinancing has rebounded slightly since the previous District report, and some of this improvement has been attributed to lower interest rates. Consumer delinquencies have increased slightly, but most respondents are hopeful that consumers' credit situation is improving. Still, banks indicated a further tightening of consumer credit standards, and credit card debt is still a concern at some institutions. Commercial delinquencies remain low.

Bankers indicate that the spread between borrowing and lending rates remains narrow, and a few are considering alternatives to traditional lending, such as investment banking and insurance, to help bolster profits.

FIFTH DISTRICT-RICHMOND

Overview: Economic activity in the Fifth District grew at a faster rate in June and July, led by stronger revenue growth in services and retail trade. Manufacturing continued to expand at a healthy pace in most industries. Commercial real estate leasing and construction increased somewhat more quickly in recent weeks while residential activity was mixed. Banks reported greater interest in residential mortgages and stronger demand for commercial loans. Although labor markets continued to be tight, wage pressures remained largely in check, except in the retail sector. In agriculture, recent heavy rains brought relief to some crops that had been stressed by unusually dry weather in June and July; however, there was flooding in some areas.

Retail Trade: Retail activity in the Fifth District experienced faster growth since our last report, particularly in the last several weeks. Revenue growth accelerated in July after growing only modestly during June. The retail labor market was exceptionally tight, with both employment and wage growth surging in recent weeks. Sales of big-ticket items and shopper traffic slowed somewhat in June, but both recovered in July.

Services: While most measures of District service-sector activity were little changed during the last two months, revenue growth accelerated sharply in June and remained strong in July. Growth in service-sector employment slowed in June, but more recently the pace rebounded. Wage growth was steady. Despite the signs of current strength, our sources again lowered their expectations of future demand.

Manufacturing: Manufacturing activity grew at a steady pace in recent weeks. Growth in shipments and new orders continued to be strong across most industrial sectors during June and July. Textile mills and furniture manufacturers, however, reported weaker demand. In North

Carolina, a textile producer noted that he lowered his prices in July and said that excess capacity "[has] resulted in intense price competition." Manufacturing employment growth has been steady since May; sources again characterized labor markets as tight, with many reporting that finding skilled workers remained their primary concern. Contacts reported that increases in their costs were outpacing their ability to raise prices.

Tourism: Tourism in the Fifth District continued to strengthen since our last report. Most sources reported that activity during the Fourth of July holiday exceeded that of a year ago, partly because of more favorable weather. A hotelier on the Outer Banks of North Carolina noted that strong bookings made it difficult for visitors without reservations to find weekend accommodations there. In mountain areas, a source from West Virginia reported that interest in white water rafting had increased and that more people were "seeking refuge from urban areas" this summer.

Port Activity: Port activity was lower in June than in May, both for containerized and break-bulk cargoes. Overall export growth moderated in June, although port representatives noted an increase in automobile, agricultural, and paper product shipments. The pace of import growth also slowed during June despite a pick-up in shipments of agricultural and wood products.

Temporary Employment: Temporary employment agencies reported that the demand for workers increased slightly in recent weeks. Most agencies continued to have difficulty filling available positions. Several agencies were actively soliciting potential employees wherever they found people gathered, including local sporting events. One North Carolina agency noted that with the shortage of computer-skilled applicants, his firm had renewed its efforts to offer workers in-house computer training.

Finance: Lending activity in the District increased moderately in June and July. Commercial lenders that we contacted reported continued strong demand for loans. Lenders cited lower mortgage rates as the major reason for increased demand for residential mortgages. Consumer loan activity was spotty. Several bankers reported an increase in loan applicants with credit problems. A Virginia banker reported that he had recently become less inclined to make loans to customers with a history of bankruptcy.

Residential Real Estate: Reports of real estate activity from realtors and homebuilders were mixed across the District. Virginia realtors reported steady sales and higher customer traffic in recent weeks. They indicated that mid-priced homes continue to sell well in most areas of Virginia. However, several contacts in West Virginia and the Carolinas reported a slowdown in home sales in their areas. A Columbia, S.C., realtor suggested that consumer credit problems were slowing activity in that market. Builders in several areas of the District reported a rise in customer inquiries, but they noted that the increased interest had not yet boosted housing starts.

Commercial Real Estate: Commercial real estate activity expanded more quickly than in May, though the pace of advance slowed from earlier in the year. Office, retail, and industrial leasing activity grew more strongly across the District amid generally falling commercial vacancy rates and rising rents. An exception to this strong picture was Columbia, South Carolina, where rents weakened. Most sources noted an increase in overall construction, although we received fewer reports of speculative construction. However, a broker in Charlotte, N.C., went against the grain, remarking that in his area, there was "more [speculative construction] than we've had here in five years."

Agriculture: Although the remnants of Hurricane Danny brought heavy rains and flooding to the District in the latter part of July, the moisture may not have come in time to help all crops. Unseasonably dry weather, which prevailed throughout most areas of the District in June and early July, had already reduced yields of corn and some other field crops. In addition, a contact in Virginia noted that the recent excessive rains would increase the threat of blue mold on tobacco crops. However, the general consensus was that, on net, the rain would prove beneficial; one North Carolina analyst stated, "the rain is going to help a lot more than it will hurt."

SIXTH DISTRICT - ATLANTA

Summary: Reports from most contacts suggest that growth remains moderate across much of the District. Manufacturing in the region has been mixed, and retailers continue to see only a modest rise in sales over last year. Realtors indicate that recent sales are near last year's strong levels, while builders say that new home construction has dipped below last year's levels in many parts of the District. However, tourism and business travel remain strong especially to destinations in Florida. Wage pressure remains subdued in most areas of the region with the exception of south Louisiana, which is experiencing a boom created by the reemergence of the oil and gas industry.

Consumer Spending: Most District retailers contacted reported that sales exceeded, in some cases only slightly, last year's levels in June and early July. Apparel sales remained strong, while sales of home-related products were mixed. Sales were generally below merchant's expectations; however, inventories are close to target. Looking forward, the majority of retailers contacted expect that third quarter sales will be up slightly compared with last year, and most expect no change in product prices over the next six months.

Construction: Overall, the single-family housing market continues to show signs of slowing. For the month of June, a majority of Realtors contacted reported that home sales were up from a year ago, but a notable minority said that sales were similar to last year. The strongest reports came from Florida. District builders generally indicated that construction was down in June and new home sales were spotty. Several said that concessions are creeping in and a significant minority of Realtors felt that there was too much construction in their markets.

District commercial real estate markets remain strong. Office markets continue to improve as vacancy rates drop, and construction remains at a brisk pace. Speculative office construction is underway in many District markets. The industrial market also remains strong across most of the region. However, lack of suitable land is slowing development in several areas. The weakest segment of the commercial real estate market continues to be multifamily housing, with several markets showing some overbuilding, declining occupancy rates, and increasing incentives to attract new renters.

Manufacturing: Reports from factory contacts are mixed, with strengthening in some sectors offsetting weakness in others. The energy sector is posting especially strong growth. A Louisiana oil rig platform fabricator says that his contract backlog has quadrupled since the beginning of 1996. New commercial ship orders, along with U.S. Navy contracts, will mean thousands of additional jobs for the region's shipyards. A spokesman for an industrial chemical producer notes that his company is operating at full capacity, and a packager is adding to employment rolls and increasing production. Industrial and commercial machinery contacts report increasing production and a positive near term outlook. Less positively, some producers of apparel report softness in the market for lightweight leisure wear, leading to further plant closings. New orders are declining for a large producer of electronic equipment, but product demand is expected to increase over the next few months. The factory workweek and shipments have decreased for some regional auto component suppliers, which one contact attributes to a softening auto market. **Tourism and Business Travel:** Reports from the tourism and hospitality industry indicate further expansion with continued strength expected. The cruise industry out of Miami is doing well, and airlines flying into south Florida are operating at capacity. Advance bookings are "looking good," according to hoteliers there. Hotels are offering fewer off-season discounts and are seeing no decrease in occupancy rates. The luxury hotel segment continues to post strong growth. In Orlando, new attractions at Universal Studios are expected to further stimulate tourism to the area. Amusement parks in Georgia and Tennessee are reporting more visitors than last year with new attractions, new rides, and no competition from Olympic events.

Financial: Bankers throughout the Southeast continue to report moderately strong loan demand with some signs of softening apparent. Consumer and auto loan demand varies across lenders, and there are intermittent reports of declines in consumer loan quality. Mortgage loan demand remains relatively flat, while commercial loan demand continues to be strong. Area banks report profits are still strong.

Wages and Prices: With a few exceptions, contacts report that wage pressures are being held in check and prices remain stable. One industry contact noted that wage increases are being counteracted by capital investment and continuing gains in productivity. Wage increases have generally been required to attract and keep qualified employees in the high-tech sector. Contacts in several parts of the region also note that their competitive environment has left them unable to increase prices to match even moderate wage increases. Labor shortages were noted in Louisiana's booming shipbuilding and marine-supply industry and by some high-tech firms in Florida. Low unemployment rates in parts of the region are reinforcing contacts' concerns of labor shortages for both skilled and non-skilled positions.

SEVENTH DISTRICT--CHICAGO

Summary. The Seventh District economy continued its moderate expansion in June and July with no new reports of upward price pressures. Consumer spending picked up from our last report as weather conditions improved, with sales slightly exceeding most retailers' expectations. Commercial construction activity continued to increase and the residential market, while softer than last year, remained strong. Manufacturing activity picked up from a brief slowdown in the second quarter, due in part to settled auto-related strikes. Lending activity was very strong in June and July and asset quality was reportedly improving. Labor markets continued to tighten and a few new reports of upward wage pressures emerged, particularly in lower-paying and clerical occupations. Recent rains helped restore favorable conditions for most of the District's developing crops.

Retail sales/consumer spending. Retail sales were described by most contacts as at or slightly above expectations over the last six weeks, and in line with their national averages. One large retailer said that no one particular product segment was doing exceptionally well or exceptionally poorly, a statement that seemed to sum up the sentiment of most other contacts. Sales of apparel, most notably women's, continued to outperform other items. A few merchants mentioned that sales of home items (big-ticket appliances, furniture, bedding, etc.) were picking up after a period of softening. According to contacts, sales of some luxury items, such as personal watercraft and all-terrain vehicles, were up noticeably over last year. Inventories were reportedly in line with most retailers' sales expectations, limiting the need for any new promotional activities. Profit margins continued to be squeezed and competition among stores remained intense. Since July is one of the slowest months for most merchants, many indicated that August sales results would be a harbinger of what's in store for the remainder of the year. One large national chain pointed out that there had been a noticeable shift recently from the use of store credit cards to third-party (Visa, MasterCard, etc.) cards. Most retailers noted that no new upward price pressures had cropped up in the last six weeks.

Housing/construction. Overall construction activity remained robust in the District through June and early July. Commercial construction activity was, as in our last report, very strong with some areas experiencing record levels of activity. The strength was nearly universal across sub-sectors. Very low office vacancy rates in many areas were spurring new office development, the bulk of which was taking place in the suburbs. A Des Moines area contact pointed to owner-occupied development as a key source of strength in that office construction market. Another contact, in the Indianapolis area, reported the first "significant" new office building in eight to ten

SEVENTH DISTRICT--CHICAGO

years. Development of light industrial and retail space continued to be strong as well. Activity in the residential real estate market, while mixed, remained strong. Construction of new homes was reportedly off 5 to 10 percent in most areas from very high levels one year ago. Building permits were down moderately from a year ago in four of the five District states, with only Iowa experiencing an increase. There were some reports of unintended inventory building and "informal" price discounting or incentives. With profit margins already squeezed and competition fierce, many builders were very reluctant to advertise discounts. Sales of existing homes picked up in June and were up moderately from a relatively soft June last year, when inclement weather hampered sales. Most realtors, however, noted that year-to-date sales levels continued to lag last year's results. Both realtors and builders expect that strong job markets and recent reductions in mortgage interest rates will keep the housing market strong through the end of the year.

Manufacturing. Manufacturing activity picked up in recent weeks after a brief slowdown in the second quarter. Many of the auto-related strikes, which contributed to that slowdown, have since been settled. A new strike, which was beginning to curtail a major automaker's production, was settled after less than a week and workers were back on the job at the time of this report. Virtually all manufacturing sectors reported increased production, strong orders, good inventories, flat prices, and high expectations. Automobile makers indicated that production had increased to the levels anticipated before scattered strikes affected output. Inventories were in very good shape, although one major producer reported a slight buildup in automobiles. Some manufacturers, however, were having difficulty keeping up with their dealers' demands for light trucks. Producers of heavy equipment, including agricultural equipment, reported strong gains in production and new orders, and inventories were mostly described as "lean". Sales of heavy trucks continued to be strong, boosting production and reducing inventories to low levels. One truck manufacturer reported difficulty in building inventories to keep them in line with higher sales. Contacts in the steel industry also reported increased production and strong orders. Prices of finished products remained flat across industry sectors with slight variations. Automobile manufacturers planned to increase slightly their use of incentives, while heavy truck makers were planning on reducing some discounts. Contacts continued to report flat to slightly lower raw materials prices.

Banking/credit. Overall lending activity remained strong, remarkably similar to that noted in our last report. Much of the strength was, once again, on the business side where demand increased steadily. Most bankers reported that the asset quality of commercial loans continued to

SEVENTH DISTRICT--CHICAGO

be exceptional and may even have improved recently. Fierce competition for C&I loans was putting pressure on pricing, but no contacts reported lowering standards to attract new loans. Lending activity on commercial real estate remained high and asset quality was generally described as excellent. One contact, however, expressed concern over a recent increase in the use of what he termed "imprudent" lending practices, such as zero-equity and non-recourse loans. Lending on the consumer side was mostly described as flat. Mortgage applications were generally down over the last six weeks. One large bank reported a noticeable increase in refinancing activity, but most indicated that rates would have to fall further before refinancing activity would pick up. Some contacts also reported increased home equity and second-mortgage lending activity. Credit card usage remained relatively flat and some banks noted that their efforts to tighten standards were paying off in the form of improved profitability.

Labor markets. In a now familiar refrain, labor markets tightened further in the District and shortages in some occupations and areas persisted. The average unemployment rate fell below 4 percent and there were a few reports of labor shortages leading to production plan alterations. There were also a few new reports of intensifying wage pressures, most notably on the lower end of the pay scale and in clerical occupations. In addition, one automaker reportedly had to raise entry level wages one dollar an hour above the going rate to fill a large number of positions. Some retailers were experiencing difficulties in retaining help. One major retailer, in an effort to reduce turnover, had recently reduced the period of time that an employee had to be on the job in order to receive a benefits package while others had to raise wages. The most severe shortages remained in the professional and technology/information occupations. The slowdown from last year's torrid pace in the housing industry had eased, but not eliminated, the shortage of construction workers in some areas, resulting in fewer project delays. Once again, contacts were careful to point out that upward price pressures remained under control.

Agriculture. Crop prices, while trending lower, fluctuated widely in recent weeks in reaction to the anticipated influence of changing weather patterns on growing crops. Favorable weather improved crop conditions in northern portions of the District during the first three weeks of July. But warm temperatures and dry soils in mid-July stressed crops in other areas, especially Illinois. Fairly abundant rains since then have helped to restore generally good conditions as the remaining bulk of the District's corn crop entered its critical pollination stage during the last 10 days of July.

EIGHTH DISTRICT - ST. LOUIS

Summary

The District economy is still growing at a moderate pace. District firms continue to report growth in sales and employment, though tight labor markets persist in many parts of the District. Contacts are generally optimistic about near-term economic conditions. Residential construction still lags last year's levels even though half of the District's metropolitan areas saw increases in their monthly permit levels in May. Total loans outstanding at large District banks rose slightly during the past two months, with commercial and industrial lending posting the largest increase. In sharp contrast to our previous report, when below-average temperatures and above-average rainfall were the norm, hot and dry weather has prevailed in most areas, causing crop and pasture conditions to deteriorate somewhat.

Manufacturing and Other Business Activity

District contacts continue to report that favorable economic conditions are allowing them to increase sales and employment, though tight labor markets still plague many parts of the District. While demand remains greatest for skilled trade workers—especially those with electronic skills, master electricians and drafters—contacts are reporting that health service workers—particularly nurses and occupational therapists—and hotel and restaurant managers are also needed. In addition, many firms are still having trouble finding and retaining qualified entry-level workers. Still, most contacts have not reported added upward wage pressure in the face of ongoing labor market tightness.

The District's furniture industry got a boost when a manufacturer decided to consolidate two of its plants into an Arkansas plant, bringing about 900 new jobs. Two new distribution warehouses will be built in the District, one that will employ almost 400 in Illinois and another that will employ about 450 in Mississippi. Truck engine and parts sales have recently exceeded expectations, according to a contact who expects this trend to continue in the coming months. Most contacts remain optimistic about economic conditions in the foreseeable future.

The District's apparel industry, however, is still experiencing plant closures because of overseas competition. For example, a shirt manufacturer closed at the end of last month, eliminating 135 jobs. In addition, the District's paper industry will shrink some as a major producer shutters two plants in a companywide restructuring. About 300 jobs will be lost at the two plants.

Real Estate and Construction

Monthly residential construction permits in May picked up in six of the Districts's 12 metropolitan areas, mostly in the southern and eastern parts of the District. Permit levels in almost all District metro areas remain below year-ago levels, which were record highs. Fort Smith and Evansville are the only District metro areas where residential construction is ahead of last year's pace. In most other cities, though, the gap has been narrowing as the year progresses. Contacts report that apartment construction is booming in Little Rock and Memphis. Other nonresidential construction also remains strong in many parts of the District.

Banking and Finance

Total loans on the books of six large District banks increased 1.5 percent between mid-May and mid-July, after increasing just 0.7 percent between mid-March and mid-May. Commercial and industrial (C & I) loans rose 2 percent in the most recent period, while real estate loans rose 1 percent. Consumer loans outstanding declined 2.1 percent. During the same period one year ago, C & I loans increased by just 0.2 percent while real estate loans rose 0.6 percent.

Agriculture and Natural Resources

In a marked departure from May and early June, when below-average temperatures and above-average rainfall were the rule rather than the exception, hot and dry weather has prevailed over much of the Eighth District over the past month or so. As a result, reports from several areas indicate a deterioration in the condition of pasture and row crops. For the time being, however, crops are generally in good condition, with most farmers continuing to expect above-average production this fall. Still, the cotton crop, owing to its slow start this spring, remains modestly behind schedule and in somewhat less favorable condition in many areas. Above-average rainfall over much of Mississippi has produced loss rates of up to 100 percent in isolated instances, leading cotton farmers to plow under their crop and replant with soybeans.

The harvesting of the District's wheat crop is largely complete. Early reports from Illinois suggest yields were above average in many areas and exceeded many farmers' expectations. Yields are expected to be above average in Indiana and Missouri also, but close to average or slightly below average elsewhere.

NINTH DISTRICT--MINNEAPOLIS

Midsummer finds the Ninth District economy experiencing continued moderate growth. Construction seems indefatigable. Despite some slowing in residential construction, employment and overall activity for the sector continue to grow apace. Sales of autos and consumer goods are solid. Manufacturers describe strong output and do not report problems with inventories or with securing inputs. Oil and gas activity is very strong. Forest products firms in the eastern part of the district report steady output, but there has been noticeable slowing in Montana. Farmers have been on a weather roller coaster, and prospects are for a good to average crop. Beef and hog producers continue to enjoy higher prices than a year ago, with output largely steady. Unemployment rates are low in most areas, and employment numbers high. Product prices show little, if any, increase.

Two areas show some problems. Output is slowing somewhat at a few iron mines in the face of higher output inventories and ongoing structural change in the steel industry. The summer season is disappointing to tourist businesses in many areas, with visitation rates somewhat below last year's levels.

Construction and real estate

"Lots of contracts," says a general manager for a commercial builder operating in South Dakota and Minnesota. Publicly let contracts in those states and in North Dakota through June ran 14 percent ahead of 1996, which itself had been considered very strong. Furthermore, there are no signs of slackening in commercial and public-sector work.

Residential permit numbers in Minnesota have slowed somewhat compared to one-year and two-year-ago levels, particularly in apartment buildings. Nevertheless, construction employment for that state is 4 percent above 1996 and 12 percent above 1995, indicating that the sector as a whole remains strong. Both commercial and residential building also continue strong in western Wisconsin and in southeastern South Dakota.

Markets for existing real estate are also brisk. "It's really a sellers' market," says one St. Paul, Minn, suburban residential realtor. Commercial property rental markets also are active.

Natural resource industries

With 28 rigs drilling in North Dakota and Montana, oil and gas exploration and development is at its highest level in more than a decade. After several years of slow decline, oil production is slowly rising as new wells come on line. Sawmills, building board manufacturers and paper mills in Minnesota, Wisconsin and Michigan's Upper Peninsula describe output as steady, but there is a noticeable decrease in forest production in Montana, with two sawmills and a cardboard plant reportedly closing. Iron mining in the Lake Superior region shows some signs of slowing after two years of all-out production. One mine is laying off 70 workers and some others are reportedly contemplating production cuts in the face of ore pellet inventories 25 percent higher than a year ago. But a steel industry source says this is more a result of continuing structural change in the sector, as minimill output continues to grow at the expense of integrated producers, and not as the result of any slowing of demand for steel products.

Manufacturing

"Good sales, we have work for some time," reports a large iron foundry manager in Minneapolis. "Somewhat better than last year," says a specialty agricultural implement builder in North Dakota. These comments are representative of many across the manufacturing sector, which seems characterized by solid, but not spectacular growth.

Agriculture

"Most of the second cutting is just junk," says an extension agent in west-central Minnesota where rains repeatedly soaked drying hay, reducing its quality. Hay supplies remain well below usual levels and prices high in many areas of the district. Farmers have been on a weather roller coaster this summer as near drought in June turned into excessive rain, hail and successive thunderstorms in July. On the whole, crops in most areas are in good, but not excellent, condition. USDA's predicted spring wheat yields for North Dakota are down about 25 percent compared to 1996 and those for Minnesota down about 10 percent. In corn-soy areas prospects are for an average crop. Hog and cattle producers continue to enjoy higher prices than a year ago, and bankers who responded to the second quarter survey of agricultural credit conditions by the Minneapolis Fed generally are more optimistic about prospects for their cattle-producing customers.

Consumer spending and tourism

"Pretty good sales, varies a bit by locality, but on the whole pretty good," is the assessment of a South Dakota automobile dealer's spokesman. "Sales are strong for most models," is the report from a dealer in Wisconsin. New vehicle registrations in most states show moderate increases above 1996 levels for the year to date.

"We are very busy," comments the manager of a Grand Forks, N.D., discount store. "People are buying lots of things to replace items damaged by the flood." Even without that special circumstance, retail sales in other areas also appear vigorous. Sales tax receipts on general merchandise reportedly are running ahead of projections in Minnesota, Wisconsin and the Dakotas. Retail chains generally report good revenues and earnings.

But tourism is the soft side of household spending. Visits at national parks and monuments in western regions of the district are trailing 1996 by as much as 20 percent. Canoe outfitters in northern Minnesota describe bookings as somewhat slack, and recurring rain storms have slowed other summer recreation activities in Minnesota, northern Wisconsin and the Upper Peninsula. Fishing resorts describe moderate, steady business. One bright spot: Large areas of open water in the prairie pothole regions of eastern North Dakota and South Dakota bode well for fall waterfowl hunting.

Employment, wages and prices

"We really need more workers," says a job service official in Grand Forks, where the unemployment rate was 2.9 percent before April flooding. "I just can't get all the people I need," says a St. Paul, commercial builder. "In our production areas, we have people speaking five languages," says an educational specialties manufacturer. "It is just hard to get people." Such labor market tightness dominated the discussion at a July meeting of CEOs from major firms at the Minneapolis Fed. Only in Montana and the Upper Peninsula are labor markets somewhat slack and unemployment rates above the national average. Employers report increasing wage pressures and renewed increases in health care costs after a two-year hiatus.

But product prices for intermediate and final goods remain quiescent. Gasoline prices have dropped a cent or two from late spring and are a few cents below summer 1996 levels.

TENTH DISTRICT - KANSAS CITY

Overview. The district economy continued to grow moderately last month, though with a few signs of slowing. Manufacturing activity remained strong and energy activity improved further. Retail sales edged down, however, and construction activity eased somewhat. In the farm economy, the winter wheat harvest was much better than last year, spring crops were in good condition, and the cattle industry benefited from high prices and excellent pasture. Labor markets remained tight in much of the district, and some companies responded by increasing wages for entry-level workers and certain skilled positions. Prices generally held steady at the retail level while increasing slightly for some manufacturing materials.

Retail sales. Retailers report sales edged down last month and were little changed from a year ago. Sales are expected to remain unchanged in the coming months. Retailers have been trimming inventories slightly but are generally satisfied with current stocks. Automobile dealers report sales were flat last month and unchanged from a year ago. Sales of light trucks and sport utility vehicles remained strong, while sales of domestic passenger vehicles were soft. Most dealers have been holding inventories steady and plan no major changes in the coming months because sales are expected to be stable.

Manufacturing. Manufacturers continued to operate at moderately high levels of capacity last month. Manufacturing materials were generally available, with lead times unchanged. Manufacturers have been trimming their inventories slightly, and some say they plan further reductions because stocks exceed desired levels.

Housing. Builders report housing starts edged down last month and were generally unchanged from a year ago. Builders expect construction activity to hold steady over the next several months. Sales of new homes were down slightly from the previous month and unchanged from a year ago. Most building materials were readily available and delivery times were normal. Mortgage lenders say demand was unchanged last month.

Banking. Bankers report that loans and deposits both increased slightly last month, leaving loan-deposit ratios little changed. Commercial and industrial loans were flat, while other loan categories showed small gains. Money market deposit accounts and demand deposits rose, outweighing declines in large CDs.

All respondent banks left their prime lending rates unchanged last month and expect to hold rates steady in the near term. Most banks did not change their consumer lending rates and anticipate no future changes. A few banks tightened their lending standards, citing concerns over credit quality.

Energy. District energy activity continued to improve last month and remained somewhat stronger than a year ago. Crude oil prices fell while natural gas prices edged up, but both oil and gas prices remained well below the peaks reached at the end of last year. The district rig count rose 3 percent in June to a level 12 percent higher than a year ago.

Agriculture. The winter wheat harvest in the district is nearly over. Crop yields are better than expected and will be well above last year's level. Wheat prices have fallen due to the larger wheat harvest, but district wheat producers will still earn bigger profits due to the good crop. Favorable weather has helped spring crops in the district develop at a normal pace, with most of the crops reported in better than average condition. Above-average yields are expected for corn and soybeans, and while larger supplies will put some downward pressure on prices, growers will likely earn solid profits.

District cattle feedlots are profitable, although a recent downturn in fed cattle prices has squeezed profits. The number of cattle in feedlots is higher than a year ago, suggesting that supplies of beef to consumers are likely to remain high and fed cattle prices could drift lower in coming weeks. Feedlots continue to market cattle as quickly as possible to stay ahead of falling prices. Meanwhile, excellent pasture conditions and high feeder cattle prices are yielding profits for most district ranchers, and ranchers are optimistic that the profits will continue this fall.

District hog producers are also enjoying a profitable year, and a new tide of pork exports to Japan may keep hog prices at profitable levels. Higher futures prices have encouraged existing hog operations to expand and large corporate farms to move into the district. While the increased production is boosting rural economic activity, many rural residents are concerned about the impacts on quality of life.

Wages and prices. Labor markets remained tight last month in much of the district, with some continued evidence of wage pressures. Employers say qualified entry-level workers and computer programmers were hard to find, and manufacturers report difficulty hiring engineers and skilled craftspeople. Some companies say they raised wages more than normal for entry-level workers and certain skilled positions, but other companies say wage increases were about normal. Prices held steady at the retail level while increasing slightly for some materials used in manufacturing. Retailers expect no major price changes in coming months.

ELEVENTH DISTRICT--DALLAS

Eleventh District economic activity picked up in June and July. Manufacturing activity increased, and demand for business services continued to increase strongly. Contacts reported that the strength of retail sales growth varied more than usual, but retailers were optimistic about the outlook. Construction activity grew at a moderate pace, while loan demand remained strong. Contacts reported that energy activity is still booming. Agricultural conditions were favorable.

Prices. Overall, there was little change in the reports of price and wage pressures. Memory chip prices are reported to be stable, but prices for some other chips declined more than expected. Semiconductor manufacturers said the labor market remained tight, but they have been able to fill most of their vacancies. Wages "are not skyrocketing," they said, but more firms are offering stock options or other nonwage benefits. Some lumber prices are up, such as oak, because of wet weather in the South and Southeast, but most are unchanged. Lower ethylene prices had been widely expected as new capacity comes on line, but following a serious explosion at the Shell Deer Park ethylene plant, supplies became very tight, prices held steady, and talk of falling ethylene prices temporarily ended. Respondents expect price increases for plastic products, but note that of the recent attempts to raise prices, the only significant increase to hold was for PET plastics for bottles. In contrast, the polyethylene price increases announced a couple of months ago failed. The energy industry continued to report solid wage gains, especially for workers with oil-field and manufacturing skills. Workers in those industries are said to be, "shopping around for wage increases," and competitors are hiring people away from each other at rising wages. Retailers said competition continued to restrain upward pressure on selling prices, although several contacts noted that competition was not as "cut throat" as it has been in the past, so "perhaps there was less discounting." New car prices are expected to increase when new models become available, but stiff competition is expected to keep used car prices soft. Most business services firms continued to report some wage pressures resulting from a shortage of qualified workers.

Fees also were up, particularly where demand was strongest, such as for accounting and computer-related fields.

Manufacturing. Manufacturing activity increased in June and July. Activity was boosted by a pickup in demand for construction-related products, boxes, and some high tech products. Demand for energy-related manufactured products continued to be strong. The summer construction season rebounded from an unusually wet spring, boosting demand for construction-related products, such as metals and brick. While demand was below last year's level, contacts generally were happy with the level of sales. Demand for liner board, an input in box production, picked up slightly and inventories of box manufacturers dropped. However, liner board demand is still below last year's level. The semiconductor manufacturing industry reported little change in activity since the last survey. Telecommunications manufacturers said demand was up for networking and switching equipment, but demand for PBX technology was flat. Demand for most energy-related manufactured products remained strong, although a poorer than expected driving season put downward pressure on wholesale gasoline prices and refining margins. Good margins this spring induced refiners to produce full-out and contacts said capacity moved close to 100 percent early in the summer. Inventories of crude and gasoline built up, but respondents noted that the futures market was providing some incentive to build inventory. Also, the July driving season seemed to open stronger than June, offering some hope for short-term stability or improvement in gasoline prices.

Business Services. Demand for business services, such as temporary staffing, legal, accounting and management consulting services, continued to increase strongly. Most respondents cited broad-based strength resulting from a strong economy. Legal firms were doing more deals to raise money for oil and gas rigs. At temporary staffing firms, demand was strongest for people with computer, accounting and engineering skills.

Retail Sales. Retailers reported sales growth, but the strength of sales varied more than usual. Several retailers said sales growth in Texas was slower than for the nation overall, but these retailers remained generally optimistic about the outlook based on the strength of national sales. Auto sales were better than expected in June and July, and contacts were optimistic about the outlook for sales growth.

Financial Services. Loan demand was strong, and bankers continued to report stiff competition, particularly for commercial and auto lending. Competition was more staid for home improvement and personal lending, however, and interest rates on those types of loans were a little higher. Competition reduced credit criteria in larger institutions and in commercial lending categories more than in consumer lending categories. Many of the smaller and rural respondents reported no deterioration of credit quality, however, and no pricing changes due to market pressures. Delinquencies also remained low, especially in the consumer lending categories.

Construction and Real Estate. Construction activity grew at a moderate pace during the last 6 weeks. Contacts reported a noticeable pick up in home sales, after slower activity from February through May. Housing construction increased, particularly for more affordable homes, although compared with last year, new home sales are flat overall. Office demand continued to be strong, pushing up occupancy rates and rents. Industrial demand was strong, with almost all new construction absorbed. Apartment demand and rents are up.

Energy. Despite lower oil prices than during the previous beige book period, oil service and machinery activity was still booming. Contacts reported that profits are high, backlogs are very large, and workers with oil-related skills are difficult to find. The U.S. rig count leveled out near 950 over the past six weeks, and respondents feel that capacity constraints for labor and equipment will limit the number of rigs that are likely to be added over the rest of the year to 50 or 60.

Agriculture. Hot, dry conditions helped spur good growth and development on spring planted crops and allowed harvest activities to make good progress. Irrigation activity increased, as well as insect activity in some areas. Disease problems also increased due to a very wet spring in many areas. Livestock conditions remained good, as did livestock markets.

TWELFTH DISTRICT — SAN FRANCISCO

Summary

Most Twelfth District contacts reported robust economic conditions in the recent survey period. Providers of business, legal, and financial services benefited from strong demand. Retail sales were moderate overall, with automobile and light truck sales falling below year-earlier levels. District manufacturing activity was high, with signs of tightening capacity constraints in some industries. Prices for real estate rose noticeably in many areas, and construction activity continued at a rapid clip. Although respondents noted shortages of skilled labor, yearly wage gains mostly were in the 3-3½ percent range, albeit with scattered reports of larger increases. Reports of upward price pressure were limited.

Business Sentiment

Survey respondents remained sanguine regarding economic prospects for the nation and the District. Two-thirds of the respondents predicted that national economic growth will proceed at its long-run trend rate over the next year, and nearly all of the remaining respondents expect growth to be above trend. Most also predicted unchanged national unemployment and inflation, although slightly over one-third expect inflation to rise. Respondents remained particularly optimistic regarding growth rates in their respective regions, with 93 percent expecting it to exceed the national growth rate over the next year.

Retail Trade and Services

Sales of retail goods were moderate overall. Automobile and light truck sales were weak, falling substantially below year-earlier levels in Utah and Idaho. Sales of most smaller retail products, such as groceries and pharmaceuticals, were moderate, but a respondent for a sporting goods manufacturer noted weak retail sales in its product lines. Respondents' characterizations of retail inventories ranged from "lean" to "higher than planned." They also noted downward price pressure on grocery products such as produce and meat, and reductions in effective prices of new automobiles and light trucks due to the impact of manufacturers' sales incentives on consumer financing charges.

Service providers benefited from healthy business conditions, as demand for business, legal, and real estate development services was strong in most areas. Energy demand was high; supply conditions varied across states in the District, due in part to energy industry restructuring. Recent tourist traffic was weak in Hawaii, but in Southern California it met normal summertime expectations and produced high hotel occupancy rates.

Manufacturing

District manufacturing activity continued at a rapid pace, although expansion has slowed slightly following an earlier surge in the aircraft and related sectors. Boeing and its suppliers have faced some constraints in attempting to meet the very high level of existing aircraft orders; the primary supply constraint in this industry has arisen from a shortage of skilled labor rather than physical plant capacity and availability of raw materials. Demand for machine tools remained strong in the District, although vigorous competition precluded significant price increases. West coast logging operations and timber mills expanded at a good clip in the first half of 1997. Light manufacturing activity grew at a strong pace in the Los Angeles area, and one respondent reported labor shortages among garment manufacturers there. Although capacity utilization reportedly rose in many industries in the District and was particularly high among paper and pulp producers, survey responses suggest only limited capacity constraints and order backlogs overall.

Agriculture and Resource-related Industries

Agricultural conditions in the District remained mostly favorable in recent weeks, with reports generally indicating good yields and sufficient demand to keep prices firm for many crops. Recent California fruit and nut yields—particularly for table and wine grapes—were enhanced by a wet January and dry weather since then. However, this weather pattern substantially reduced wheat production in the state. Sales of Idaho potatoes remained weak, although other crops did well there. Cattle prices firmed further, due largely to demand that exceeded 1996 levels. District seafood yields were low.

Real Estate and Construction

Real estate markets and construction activity reportedly were healthy in most areas of the District. Although residential housing markets in the San Francisco Bay Area remained hot and markets in most other areas of California firmed further, markets in Los Angeles and a few inland areas in the north and south remained favorable to buyers. Nonresidential construction activity was strong in many areas of California. However, in the San Francisco Bay Area (outside of Silicon Valley), prices for commercial property have not yet been sufficiently attractive to generate substantial new commercial construction, and in Los Angeles the departure of several corporate headquarters from the area has offset factors working to firm commercial markets there. Reduced construction and sales were evident in Utah and Idaho, although activity remained at high levels. In Washington, Oregon, Arizona, and Alaska, residential and commercial construction, sales, and prices rose, particularly in major urban areas. In several areas of the District, sustained expansion of building activity has led to shortages of skilled construction labor and rising construction costs.

Financial Institutions

District banking conditions were healthy in recent weeks. Loan demand growth remained strong overall, picking up in Southern California but slowing in several states where economic growth has slowed. Credit quality was stable. Deposit growth reportedly has been limited by favorable returns in equities markets.