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Summary of Commentary on _____

Current Economic Conditions

by Federal Reserve District

October 1997

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

October 1997

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SUMMARY*

Most District reports characterized early autumn's economic activity as moderate to strong in most areas. Retail sales in most Districts in September were weaker than anticipated, with some pickup in October. Automobile sales were mostly slower. Manufacturing activity accelerated or remained at high levels for most Districts, and the outlook was generally positive. Despite the residential real estate markets' recent uneven performance, activity remains at elevated levels overall, and most commercial real estate markets continue to perform at strong levels. The energy extraction sector continues to strengthen. Labor shortages have intensified for key sectors, such as the high-tech and energy extraction industries. Yet, reports of increasing wage pressures are infrequent. Prices remain stable, as competitive factors and resistance from buyers are making it difficult for producers to pass on any cost increases. As harvesting progresses, recent rains have had varying effects on crops nationwide. Commercial lending remained strong in many Districts, while consumer lending was more mixed.

CONSUMER SPENDING

Most Districts report that retail sales were mixed during September and early October. Atlanta, Chicago, Dallas, New York and Philadelphia said that sales did not meet some retailers' expectations, and sales declined in Philadelphia. Atlanta, Chicago, Cleveland, New York, and Philadelphia merchants said that unseasonably warm weather put a damper on sales in September,

*Prepared at the Federal Reserve Bank of Atlanta and based on information collected before October 20, 1997. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

particularly apparel. However, in the Chicago, Cleveland, Dallas, and New York regions the advent of cooler weather in October reportedly has boosted sales.

Retail sales growth remains moderate in the San Francisco District despite slow apparel sales in parts of the District. In Minneapolis, recent sales have been good with back-to-school sales stronger than normal.

In the Atlanta District, home-related product sales were strong and, in New York, several retailers noted a resurgence in home goods sales. Appliance sales were said to be strong in both Boston and Cleveland. In Richmond, however, big-ticket items weakened further. In most Districts, retail inventories remain at desired levels.

Looking toward holiday sales, retailers in Atlanta, Chicago, Kansas City, and Dallas are optimistic concerning their prospects. Many retailers note their only concern is finding seasonal employees.

Most Districts reported that automobile sales were down at least slightly. Total automobile sales were down in the Cleveland, Kansas City, and Philadelphia Districts, although demand for light trucks and sports utility vehicles remain strong in Kansas City and Philadelphia.

TOURISM AND CONVENTION BUSINESS

Tourism appears to have strengthened from a year ago, according to most reports. Tourism spending has recently picked up in the Minneapolis District. Mild weather has boosted visitors to attractions in the Richmond District. Travel and tourism is strong in California and Utah, although fears of El Nino have caused some cancellations for the winter season. Atlanta reports that in Florida, room rates are up and hoteliers are encouraged by advance bookings. Cruise ship vacation demand out of Florida is up with unusually high levels of bookings.

MANUFACTURING

Manufacturing activity continued to grow in many parts of the country. Plants were operating at high levels relative to capacity in the Kansas City, Chicago, Dallas, and Cleveland Districts. St. Louis and Minnesota report healthy sales by manufacturers. In San Francisco, wood product production and expansions in food processing are occurring in addition to the strong growth in aircraft and high-tech equipment. San Francisco also reports transportation shortages, causing difficulties for production and delivery. Richmond notes that growth in shipments increased in many industrial sectors, and New York reports a broad improvement in the region's manufacturing sector. In the Boston District, makers of aircraft parts and computer-networking equipment are posting rapid growth, and the semiconductor industry is increasing production. In Minneapolis, computer-related producers are also doing particularly well. Production of heavy equipment is accelerating from already high levels in Chicago. Dallas and Atlanta report that demand for oil and gas equipment also remains strong. Increased sales are prompting plant expansions and employment gains in the St Louis region's factory sector. Steel plants are operating at high levels in the Chicago District and the strength is expected to last for the remainder of the year. Atlanta reports that new contracts have spurred shipyards to operate at capacity levels. Atlanta and Boston also note that factory contacts are mostly optimistic that the coming year will see a continuation of current trends in the manufacturing sector. Less positively, Minneapolis reports that restructuring continues to result in significant layoffs in their factory sector, and weakness persists in Atlanta's large apparel sector.

REAL ESTATE AND CONSTRUCTION

Residential construction and sales have been uneven. Chicago noted a pick up in construction and new home sales. An unexpected demand for housing also boosted residential homebuilding in Dallas. In the Richmond District, homebuilding starts have been flat to down recently. Construction is said to be down from last year's levels in Kansas City and St. Louis, while homebuilding is characterized as generally strong in Minneapolis and San Francisco.

Commercial construction continues to grow. In Boston and Chicago, construction of most types is at higher levels recently. Office markets in Atlanta, Dallas, and San Francisco continue to tighten. Industrial space is difficult to find in areas of Atlanta, Minneapolis, and San Francisco. However, in Dallas, new supply is expected to exceed demand by year-end. In Minneapolis, many firms are planning expansions.

FINANCIAL SERVICES

Overall, bank lending was mixed across Districts and loan types. Commercial loan demand increased in many areas of the country. Cleveland, St. Louis, Philadelphia, Kansas City, Atlanta, and Chicago reported that commercial loan demand continued to grow. Consumer lending slowed in Atlanta, St. Louis, Cleveland, and Philadelphia but increased in New York and Richmond. Residential mortgage demand was described as strong in Chicago and Richmond, up slightly in Atlanta, and slowing in Dallas. Mortgage refinancing continued to increase in New York and Richmond, while holding at a constant level in Cleveland.

Bank credit standards remained steady in Cleveland and increased in Philadelphia and Chicago. Some of the slowdown in consumer borrowing has been attributed to the deterioration

in consumer balance sheets and increased credit restrictions, according to reports from the Atlanta and Philadelphia Districts respectively.

AGRICULTURE AND NATURAL RESOURCES

Good weather helped the harvests in Chicago, Minneapolis and San Francisco. Recent rains were too late to offset the drought damage to the corn crop but helped soybean, cotton, and peanut yields in Richmond. Rainfall also assisted small grains and winter pastures in Dallas. However, heavy rains have caused concerns about the cotton crop in St. Louis. Harvesting was slowed in San Francisco by shortages of seasonally employed laborers and fierce competition for transportation needed to get harvests from field to market. Scattered instances of rural rail disruptions were reported in Chicago and in the St. Louis District. They have hampered some crop shipments. Oil and gas industry activity is increasing in the energy producing regions of the nation.

WAGES AND PRICES

Many Districts report tight labor markets and hiring difficulties in some occupations, but there are few reports of wage or price pressures. In Dallas, business service firms' revenue growth has slowed because there are not enough workers to meet increasing demand and, in San Francisco, a shortage of skilled workers is beginning to limit activity in some industries. Temporary employment agencies in Cleveland are having trouble meeting demand. Job turnover in the Minneapolis/St. Paul area is reportedly nearing 30 percent. A contact in Chicago notes that some manufacturers are "desperately short of people," especially for entry-level positions, and retailers in that District are already concerned about finding holiday help. A severe shortage of people with technical and computer skills is hurting some companies in the Atlanta District.

Atlanta and St. Louis report that some companies are trying to encourage job training that would better address current business needs. Although increases in wages generally remained limited to computer-related occupations or those in the energy extraction industry, several Districts noted growth in other forms of compensation, such as expanded merchandise discounts, benefits for seasonal workers, and referral awards. Prices of inputs and finished goods remain stable for most Districts.

FIRST DISTRICT - BOSTON

The First District economy continues to expand at a moderate pace, with contacts in manufacturing, retailing, and insurance reporting revenue growth. Respondents say labor market tightness is confined to selected submarkets and is not translating into general wage acceleration; they cite wage and salary increases of 3 to 5 percent. Prices of inputs and finished goods reportedly remain stable, with only a few exceptions. A local forecasting group expects the region's rate of job growth to slow over the next couple of years, in line with the nation's.

Retail

Most retail contacts report that sales continue to grow reasonably well in the current quarter. Areas of strength are women's apparel, tourism, and office and graphic reproduction supplies. These sectors report growth in the 5 to 10 percent range, a deceleration from the 10 to 15 percent growth reported earlier this year. Areas of weakness continue to be men's and specialty apparel. Appliance contacts report high single-digit sales growth, reversing reports of declines earlier in the year, but they say this recovery may be attributable to significant consolidation of appliance retailers in New England rather than rebounding demand.

Employment is said to be either increasing modestly or holding steady, with headcounts rising where sales are strongest. Some respondents report pockets of tightness in labor markets, most notably in stores selling high-end apparel or office supplies and in low-skill areas related to tourism. Other contacts holding employment steady cite no difficulty in hiring for turnover. Even where labor markets are tight, wage inflation is not picking up; wage increases are in the 3 to 5 percent range.

Respondents report that prices are generally holding steady, although one seller of men's specialty apparel is reducing prices to move inventory. Most contacts say that profit margins are unchanged or increasing slightly, with the increases attributed to efficiency improvements such as better inventory control,

automation, and purchasing efficiencies. With the exception of building materials, for which vendor prices are up about 3 percent, most contacts say that materials costs are also holding steady. Looking forward, retailers expect steady growth at a modest pace continuing through the first quarter of 1998.

Manufacturing

Most of the First District manufacturers contacted report that recent revenues are up from a year ago, typically at a single-digit rate. Makers of aircraft parts and computer networking equipment are experiencing the most rapid growth. The semiconductor industry is reportedly ramping up production after its recent slump. Firms supplying automotive components are doing well, but one contact notes that U.S. automakers are sharply reducing new orders for capital goods from domestic suppliers. Some producers of consumer items indicate that sales are being limited by conservative stocking at retail. Many manufacturers are selling a rising share of their products overseas, although some say the strong dollar is holding down reported international revenues.

Most respondents report that, overall, both materials costs and selling prices continue to be essentially flat. Paper prices are firming somewhat, and paper product manufacturers have increased selling prices a little. A few contacts report small price increases associated with product improvements or strong demand in certain niches.

Employment trends vary widely. However, companies that have expanded or contracted noticeably over the past year now tend to report that their head counts are stabilizing. Manufacturers generally cite average wage and salary increases in the range of 3 to 5 percent, with strong upward pressure in computer-related occupations. On balance, contacts report that it is taking longer to fill openings in information systems, engineering, and accounting positions, especially in out-of-the-way locations.

Manufacturers mostly appear optimistic or at least hopeful that the coming year will see a continuation of current trends. Respondents selling innovative products and those tapping into growth markets are especially upbeat.

Commercial Real Estate

The commercial real estate market in New England is doing well. Contacts report high levels of activity in most areas, with generally lower vacancy rates and only small price increases. An exception is the Greater Boston area, where rental rates have increased significantly. Several contacts express surprise at the lack of new construction, given the high activity levels.

Conditions vary across the region, with a vacancy rate of 5 percent in the downtown Boston office market, and 25 percent in the Greater New Haven office market. After six months of little activity, Maine has reportedly picked up in the third quarter. Rhode Island is also doing well, particularly the industrial and suburban office markets. Conditions in Connecticut are mixed, although vacancy rates have declined slightly. Respondents are optimistic about the rest of the year, with most predicting some new construction "soon."

Nonbank Financial Services

Respondents at insurance companies report increases in revenue in the range of 10 to 20 percent in the third quarter of 1997 compared to the third quarter of 1996. New sales were due mostly to mutual funds, variable annuities and variable life insurance. Employment is increasing at the majority of respondents. Contacts note continued shortages of technology personnel. While most wages and salaries at insurance companies are rising at a 4 percent pace, compensation for computer programmers is up 8 to 10 percent.

The Outlook

The New England Economic Project (NEEP), a nonprofit forecasting group, released its semiannual five-year regional forecast in mid October. NEEP expects employment growth to slow from its current 2 percent annual pace, averaging 1.5 percent over the 1997-2001 forecast period. Services and wholesale and retail trade will continue to account for most of the region's job growth; manufacturing job losses will be very gradual. The regional unemployment rate is expected to deviate very little over the forecast horizon from its recent 4.0 to 4.5 percent range.

SECOND DISTRICT--NEW YORK

Economic growth in the Second District has moderated since the last report. Major retailers report that sales were below plan in September and early October, but seemed to be picking up at mid-month. The New York area's office markets continued to tighten in the third quarter, but housing markets were mixed. Regional purchasing managers' reports indicate a pickup in manufacturing activity in September. There was no evident pickup in price pressures in the District. Finally, local banks report that both loan demand and delinquency rates were steady.

Consumer Spending

Most major retailers in the region report that sales were well below plan in September and early October, though most note an incipient pickup in business in mid-October. Compared to a year ago, same-store sales in September ranged from a 4 percent decline to a 6 percent rise. The weakness was largely concentrated in seasonal merchandise and attributed to unseasonably warm weather; similarly, much of the mid-October pickup was attributed to the onset of cold weather. Still, most contacts sense some weakening in underlying demand. Much of the weakness was concentrated in apparel; only one contact reported a discernible impact from New York State's week-long waiver on moderately priced clothing (in early September), but even in that case, monthly sales were soft. A few retailers noted continued recovery in sales of home goods.

Despite the recent sales slump, inventories generally remain at satisfactory levels. Although there are a few pockets of surplus seasonal merchandise, these are expected to be depleted once the weather cools. One contact, however, expressed concern that a repeat of September's slump would be "disastrous". Some retailers report less discounting than a year ago, while others report increasingly aggressive markdowns due to the recent softness; on balance, though, merchandise costs and selling prices are said to be essentially flat. There has been no noticeable increase in retail wage pressures (nor

any reported effect from the recent minimum wage hike); however, most retailers note the real test will come in the next few weeks when most of the industry's holiday-season hiring is done.

Construction & Real Estate

Office markets continue to tighten across most of the New York City metro area. Manhattan's office availability rates fell during the third quarter—Midtown's edged down from 11.3 percent at the end of June to 10.7 percent at the end of September; Downtown's fell from 21.0 to 19.2 percent; and Midtown South's tumbled from 9.5 to 7.3 percent. Rates also declined in Fairfield and Westchester Counties but edged up on Long Island. Meanwhile, asking rents have begun to accelerate in Downtown Manhattan and Fairfield County, and continued to rise at a 5-6 percent pace in Manhattan's Midtown and Midtown South areas. In Long Island and Westchester, rents remained steady.

The region's housing market has been mixed since the last report. Builders in upstate New York say the market remains soft but has apparently bottomed. Construction activity reportedly remains weak in the Rochester, Buffalo and, especially, Syracuse areas; however, there has been some pickup in the Albany area and some pockets of strength are reported outside the major metropolitan areas—for example, in the mid-Hudson Valley, Saratoga and the Finger Lakes regions. Homebuilders in downstate New York, especially Long Island, say the market remains strong, especially at the high end. Similarly, while New Jersey builders specializing in mid-priced homes give mixed reports on the market, those at the high end report strong demand; remodeling activity remains exceptionally strong.

New York State Realtors report that the market for existing single-family homes cooled a bit in the third quarter—unit sales were down 4 percent from a year ago in August, with most areas posting declines. Average selling prices were up 5 percent statewide, with all of the increase concentrated downstate. However, a large Manhattan broker reports that co-op and condo prices retreated in the third quarter following a springtime surge; the average price per room is little changed from a year ago.

Other Business Activity

Regional purchasing managers report broad improvement in the region's manufacturing sector, along with an absence of price pressures in September. Buffalo purchasing managers report that new orders accelerated further in September, while production activity continued to expand at a brisk pace; however, there was little change in hiring activity and commodity price pressures remained modest. Similarly, Rochester purchasers report a sharp improvement in general business conditions but a dip in employment and stable prices. New York purchasing managers in both the manufacturing and non-manufacturing sectors report that business activity accelerated in September and that prices paid for goods and services remained flat.

Regional labor markets continue to improve gradually. New Jersey payroll employment, which is growing at a roughly 1.5 percent pace, surpassed its pre-recession peak in September. Job growth remains mixed in New York, with upstate continuing to lag the New York City area. Eastman Kodak, which employs nearly 35,000 people in the Rochester area (about 7 percent of the local workforce), announced that it will cut 10 percent of its jobs this year, including 20 percent of management jobs.

Financial Developments

According to a survey of loan officers at small and medium sized banks in the District, overall demand for loans remained relatively stable during the past two months, though demand for consumer loans increased slightly. Refinancing continued to increase. Willingness to lend increased, with 29 percent of bankers reporting more willingness to lend, and none reporting less. Credit standards on all categories of loans remained unchanged over the past two months.

Interest rates decreased for all types of loans—most notably for residential mortgages, with 62 percent reporting lowering rates; however, deposit rates remained mostly unchanged. Delinquency rates remained stable over the last two months.

THIRD DISTRICT - PHILADELPHIA

Business activity in the Third District was mixed in September and early October.

Manufacturers reported continuing moderate gains in orders and shipments, although they did note some slight declines in employment. Retailers have been adversely affected by abnormally warm weather that has delayed consumers' fall clothing purchases and, in the opinion of some merchants, other shopping as well. Auto dealers also noted that sales have slowed in the past several weeks. Bankers generally reported a dip in consumer lending, which they attribute partially to a slackening in consumption spending and partially to more restrictive credit standards. Commercial and industrial lending has moved up slightly, and banks and other lenders continue to promote business loans aggressively.

MANUFACTURING

Reports from Third District manufacturers contacted in early October indicated that moderate growth continued in the region's goods-producing sector. Around one-third of the firms said they have been getting increased orders in recent weeks, although one-fourth said orders for their products have slipped. Producers of chemicals and machinery generally said demand for their products was good, but lumber and metal producers said orders have been declining. There was little evidence of capacity pressures in the District's manufacturing sector. On balance, order backlogs were declining at area plants and delivery times were getting shorter. Most firms reported steady rates of working hours, although some firms reduced work forces.

More than three-fourths of the firms surveyed said both input and output prices have been

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steady. The number of firms that have raised their prices recently was offset by an equal number that cut prices. Although manufacturers who reported recent increases in input costs outnumbered those noting decreases, in general, firms in the District have been holding the line on the prices of their own products. Plant managers say price resistance from the buyers of their products has prompted them to look for and implement more efficient production methods to offset increases in the costs of raw materials.

RETAIL

Retailers contacted in mid-October indicated that sales, in current dollars, were below the year-ago level in September and the first half of October. The normal fall pickup in sales has been delayed, according to store executives, because of unusually warm weather during this period. Consumers have postponed purchases of fall apparel and outerwear. In addition to clothing stores, many department stores and general merchandise stores have not met sales plans as a result of weak apparel sales. For some stores the shortfall has been significant. Some merchants believe that consumers who have put off apparel purchases have cut back on shopping trips and reduced other buying as well. Colder weather was beginning to enter the region in mid-October, and retailers expressed hope that fall shopping would pick up with the return to more seasonal temperatures. In general, merchants believe consumer confidence has not ebbed, and they have not altered their fourth-quarter sales goals.

Auto dealers said that sales slipped in September from August and had not picked up yet in October. While sales of sport utility vehicles have been good, a drop in sales of sedans has pulled down overall auto sales. Similarly, overall inventories have risen above desired levels. Dealers and manufacturers are offering larger rebates and other incentives in order to boost sales.

FINANCE

Total loan volumes at major banks in the Third District edged down in September. Small gains in commercial and industrial lending were offset by drops in consumer and real estate loans. The increases in lending to business have come from stepped-up marketing to smaller companies and increased usage of credit lines by existing customers, primarily for working capital to support growing business activity. In addition, there were some reports of increased international financing activity. Bankers continue to describe commercial loan pricing and other underwriting terms as very competitive among banks and nondepository lenders. In contrast, although promotion of credit cards continues to be extensive, some banks have implemented stricter terms for credit cards and other forms of unsecured lending. These include more stringent credit qualifications and lower credit limits. Bankers believe that these credit limitations and a pause in consumer spending have both been factors in the recent slowing of borrowing by individuals.

PRICES

Price pressures in the region have shown no appreciable change recently, according to business contacts. Most of the manufacturers contacted for this report said both input and output prices have been steady. Those firms that have experienced some increases in input costs also indicated that they have been unable to pass these increases on in the prices they charge for the products they make. Retailers reported that price competition among stores remains strong and that consumers are quick to shift their patronage to lower price sellers for any given product. Some merchants noted that offering attractive prices will be an important component of their marketing strategies during the upcoming holiday shopping period.

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FOURTH DISTRICT - CLEVELAND

General Business Conditions

District business conditions remain strong overall, with modest growth noted in production, orders, and employment for a variety of industries. Price and wage increases continue to be slight, and unemployment is extremely low in many areas.

Temporary employment agencies are having difficulty meeting demand; a few of them report as much as a 20% increase over the previous month as employers step up seasonal hiring. Information analysts and workers for light industry are in great demand. The agencies also report increased recruiting costs. However, with the notable exception of rising salaries for workers with computer skills, no general increase in wages is seen.

Organized labor reports little change from the current compensation growth trend of about 3% per year. In some cases, union contract terms have been extended to four and five years, from their more traditional two- and three-year lengths. Job security remains a focal point in labor negotiations as companies increase outsourcing, overtime, and the use of temporary workers.

Manufacturing

Manufacturers sustained their high output, and in some cases production strengthened a bit in September and early October. In fact, orders growth appears to have improved across a range of industries, and the orders backlog has increased slightly. Auto suppliers indicate a brisk production pace and heavy truck manufacturing is reported to be quite high. Finished goods inventories are thought to be moderate relative to sales and down slightly from midsummer.

Manufacturers report generally flat commodity prices, with the exception of a slight decline in copper. Finished goods prices are also holding nearly steady. Shortages of certain workers—especially of unskilled labor—were noted, although none of the manufacturers contacted indicated upward wage pressure.

Consumer Spending

Retailers in the District report that sales in September were down from August and they blame unseasonably warm weather for weak apparel sales. However, retail sales are thought to have improved during the first two weeks in October, leading many retailers to anticipate a solid sales rebound this month. Recent sales growth has been led by appliances, telecommunications equipment, and toys.

Inventories are considered to be “in good shape,” helped partly by improved inventory management systems. Some District retailers see competitive pressures holding down price increases and do not note any large price increases from suppliers.

District auto sales were off between September and early October, perhaps because of generous end-of-summer incentives designed to clear out the remainder of the 1997 model year. Most dealers expect sales to improve with the introduction of new models, for which a few specific shortages are already being seen.

Agriculture

The District’s harvest of traditional crops is nearly complete. Drier weather in recent weeks has been ideal for harvesting, and farmers have already planted about half the winter wheat. Late plantings, combined with this summer’s high temperatures, have resulted in an uneven corn crop. Kentucky and Pennsylvania’s yields are almost certain

to be less than 1996, whereas corn output in Ohio is expected to be as much as 50% above last year. Kentucky livestock farmers expressed concern that low corn yields may force them to buy additional feed this winter, further reducing their profit margins.

Soybean production in the District is expected to be 19% higher than last year. In fact, Kentucky's crop should be the largest in 15 years. District-wide, 90% of the tobacco crop has been cut and the forecast for tobacco production is 11% higher than 1996 and its best showing in three years. Despite some adverse weather and localized diseases, 84% of this season's crop is rated as good to fair, and 10% as excellent.

Corn prices received by farmers in September were mixed compared to the previous month (higher in Kentucky and Pennsylvania and lower in Ohio). District farmers saw soybean prices fall between September and August.

Banking and Finance

Lending activity in the District remains varied between commercial and consumer loans. Commercial loan extensions are holding steady at a good level, and a few banks even report a slightly stronger market. Consumer loan growth is still soft, however. Some banks also note a shift from consumer loans toward home-equity loans. Mortgage refinancing activity is reported to be constant at an average level for the season.

Competition for borrowers is fierce, and the spread between borrowing and lending rates remains very narrow. Many medium and small banks report added competitive pressures from credit unions. The market for auto loans has been a particularly active area for credit unions. Credit standards are described as holding steady, although consumer credit delinquencies are still on the rise.

FIFTH DISTRICT-RICHMOND

Overview: Fifth District economic activity expanded moderately from an already high level in September and early October, amid increased reports of capacity constraints in some sectors. Manufacturing output surged, while growth eased somewhat in the retail and services sectors. Banks reported generally stronger loan demand, particularly for home mortgages. Commercial real estate activity remained robust, but growth in the residential market showed signs of slowing. Labor markets tightened further and moderate wage pressures persisted. Prices, however, were little changed. In agriculture, October rains helped to alleviate drought damage to hay and some field crops.

Retail: The pace of retail activity in the Fifth District eased since the last Beige Book. Revenues grew during September, but at a much lower rate than in August. Employment in the retail sector fell. Contacts, however, reported difficulty finding and retaining workers, and wage growth was notably stronger. Sources noted that shopper traffic was little changed from August. Retail inventories grew more slowly than in our last report while sales of big-ticket items weakened further. Retail prices remained stable.

Services: Service sector activity expanded at a somewhat more modest pace in September. Revenue growth at service sector firms slowed. Employment in the service sector increased, but compared to August, the gains were more modest and sources noted a greater shortage of qualified workers. Wage growth eased slightly from August. Looking forward, service providers were more optimistic about future business conditions; most anticipated increased demand for their services through the first quarter of 1998.

Manufacturing: Manufacturing activity strengthened in recent weeks as growth in shipments and new orders surged in many industrial sectors. The industrial machinery, transportation equipment, rubber and miscellaneous plastics, and primary metals sectors experienced the strongest growth in September, while the printing and paper products sectors experienced the weakest growth. Contacts in the furniture industry reported a slight moderation in shipments; one manufacturer said that continued weak sales had led to capacity underutilization at her firm. Other furniture industry contacts, however, suggested that demand at their firms was rebounding. The level of manufacturing employment changed little. Sources continued to note

severe shortages of skilled labor, particularly of machine operators. Compared to August, wages grew at a slightly higher rate, although prices grew at about the same rate.

Tourism: Tourist activity continued to strengthen in September and the first half of October. Most respondents indicated that exceptionally mild weather boosted activity above year-ago levels. A hotelier on North Carolina's Outer Banks noted that his business had experienced the best September and October in a decade. A source from West Virginia reported that heightened interest in white water rafting, canoeing and falconry had increased the number of visitors at his resort during September and October.

Ports: Port activity slowed somewhat since our last Beige Book with declines in import and export volumes. Both containerized and break-bulk cargo shipments edged downward. Contacts reported stronger growth in automobile and paper products shipments, but noted slower growth in agricultural commodity shipments.

Temporary Employment: The demand for temporary workers continued to increase during September and early October. Contacts at temporary employment agencies said that filling open positions had become more difficult, especially for jobs requiring expertise in specialized computer software. One source said that, because of strong demand for their products, businesses no longer had time to train workers. Several other sources reported that they could no longer find "idle bodies" to put to work, but instead were relying on workers who were interested in changing jobs. As one put it, agencies in her area were now just "reshuffling the same deck." Wage growth picked up in some metropolitan areas during early September, but then appeared to moderate in early October. Contacts expected wages to remain fairly stable until year's end, but felt that wages could rise further early next year.

Finance: Lending activity at Fifth District financial institutions strengthened in September and October. Several contacts stated that lower interest rates on mortgages had increased customers' interest in fixed rate mortgages and led to a pick-up in refinancings. A North Carolina banker reported an "explosion of activity" in the home mortgage market. In commercial lending, stiff competition for accounts continued, with interest rates and other terms becoming more favorable to borrowers. Consumer lending was generally higher; one source reported a very strong increase in consumer lending activity at his institution due to a successful in-house promotional campaign.

Residential Real Estate: Residential real estate activity was steady across much of the District in recent weeks. Most contacts reported little change in home sales and customer traffic. A Greensboro, N.C., contact commented that the market there was “not real active, nor was it real bad.” Homebuilders generally reported either flat or declining housing starts in their areas. A builder in the Hampton Roads area of Virginia indicated that residential construction was not faring well in his area, while a North Carolina contractor said that some overbuilding might be occurring in that state. Although most building construction costs held steady, several builders noted that lumber prices had risen in recent weeks.

Commercial Real Estate: Commercial real estate activity in the Fifth District remained strong since the last Beige Book. The level of leasing activity changed little from August; some realtors, however, said that they were seeing leasing activity moderate somewhat because of a lack of available space. In most areas, low vacancy rates and healthy rent levels held steady. Contacts reported that rents were moving higher in a few cases, but noted that outside of the Washington, D.C., area, the increases were “nothing extraordinary.” There were only scattered reports of new construction; some sources said that given the amount of commercial space currently in the pipeline, many developers were taking a “wait-and-see approach” before starting additional projects.

Agriculture: The arrival of much-needed rains across most of the District in October improved the late-crop yield prospects somewhat according to agricultural analysts. Although not in time to offset drought damage to the corn crop, recent rains assisted soybean, cotton, and peanut yields, though not enough to raise them to normal levels. In addition, the rains boosted prospects for a late hay cutting and lessened livestock producers’ fears of a critical hay shortage this winter. Such fears had prompted some District cattle producers to move up the marketing of their cattle, leading to lower-than-usual-market weights in recent weeks. In the fishing industry, an outbreak of the pfiesteria organism temporarily closed down commercial fishing on several rivers that drain into the Chesapeake Bay. The impact on the overall catch was not substantial, although demand for seafood was reported to be sharply lower.

SIXTH DISTRICT - ATLANTA

Summary: The Southeastern economy continued to post moderate growth into early fall, according to most contacts. Merchants report that sales are up from a year ago, and they are optimistic about the holiday sales season. Home sales and construction weakened slightly, while commercial real estate occupancy levels and building are increasing. Factory activity is mixed, but contacts are positive about long-term prospects. Commercial loan demand is stable, while consumer loan demand varies by location. The tourism and hospitality industry continues to register strong numbers and a bright outlook. Wage pressures are limited to a few industries, even though labor markets remain tight in several parts of the District. The outlook for material and finished product prices over the next few months is for little change, according to most reports.

Consumer Spending: Although most District retailers reported that sales in September exceeded year-ago levels slightly, almost half said that recent sales had not met their expectations. On a year-over-year basis, sales were generally stronger in September than in August. Several retailers attributed the dip in August sales to the unusually early start of schools, which shifted purchases into July. Home-related product sales were strong across much of the District, while apparel sales were decidedly mixed by location. Warm temperatures stalled fall apparel sales in many parts of the District. Looking forward to holiday sales, many merchants are optimistic about the fourth quarter.

Construction: Home sales and construction were mixed around the District during August and September. However, both were slightly weaker in September on a year-over-year basis than August. Inventories remain generally in good shape. Realtors indicated that no overbuilding was

occurring in their markets. Builders and Realtors expect residential home sales and construction in the remainder of this year to be about unchanged from last year.

District commercial real estate markets remain healthy. Most suburban and central district office markets continue to report rising occupancy levels and rental rates. A good deal of speculative construction is underway. The industrial market is near “equilibrium” throughout much of the District. Despite declining occupancy rates and the presence of concessions in several District markets, multifamily construction remains at high levels.

Manufacturing: Although more factory contacts reported some recent slowing in current production, the number expecting production, new orders, and factory payrolls to increase was up significantly. Companies, other than apparel firms, are reportedly responding to strong demand by continuing to invest in high-tech equipment to boost production. Orders are increasing for plywood producers, building products firms, and a manufacturer of appliances. Shipyards are operating at 100 percent capacity, and backlogs are increasing because of new contracts. Activity in the oil and gas sector in Louisiana remains strong, and industry experts anticipate that the upturn will continue for a considerable length of time. Some regional military contractors are increasing capital expenditures. Less positively, however, weakness persists in the Southeast’s large apparel sector. About 4,700 jobs have been lost by Georgia apparel producers alone over the year. The factory workweek has also recently declined for auto producers. Slower sales have forced some regional auto plants to cut back production shifts.

Tourism and Business Travel: The outlook remains positive in the tourism and hospitality sectors. Room rates are up and hoteliers are excited about advance bookings in central Florida. In south Florida, hotel and motel occupancies reportedly continue to outpace record year-ago

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levels. Cruise ship vacation demand is up with an unusually high level of bookings and deposits. Capacity has increased substantially. The strengthening dollar, however, is adversely impacting European inbound traffic to Florida. Convention activity is up from a year ago in Atlanta. Attendance and revenues have picked up for some of Mississippi's gaming establishments, indicating that recent declines in casino activity may have been only temporary.

Financial: Commercial loan demand has remained stable in the District, while consumer loan demand has slowed in some locations. Mortgage applications are up slightly, and automobile loan demand is flat. Bankruptcies are still problematic, and some slowdown in consumer borrowing has been attributed to the deterioration in consumer balance sheets.

Wages and Prices: Labor shortages continue to be reported in parts of the District, but reports of wage pressures are infrequent. One contact notes that the scarcity of workers is forcing companies to automate their processes as much as possible. Another reports that it will be hard for his company to grow unless the "severe shortage of technical workers" eases. More companies are reportedly getting involved with technical and trade school faculties to focus curriculum thereby increasing the firm's potential labor pool. Contacts note that apparel employees are more concerned about job security than wage increases in light of the closings of a number of mills.

Prices are generally stable. Most contacts report that they are unable to pass increases at the input level on to end users because of competitive factors. In Louisiana, costs in the oil and gas sector are rising notably.

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SEVENTH DISTRICT--CHICAGO

Summary. The Seventh District economy continued its moderate rate of expansion in September and first half of October while prices remained in check. Retail sales were hampered by unseasonably warm weather, but showed some improvement as temperatures cooled in mid-October. On the other hand, warm weather was attributed for boosting new home sales and overall construction activity in the District. Manufacturing production continued at very high levels and new orders remained strong. Lending activity was again mixed by market segment, with the business side stronger than the consumer side. Labor markets continued to tighten and there were a few new reports of intensifying wage pressures, most notably in rural areas. Warm, dry weather permitted faster-than-normal progress with the fall harvest, yet grain prices rose contra-seasonally because of uncertainty over China's grain production and the effects of El Nino on tight world grain markets.

Consumer spending. Retail sales in the District were below most merchants' expectations but in line with national results. Unusually warm weather in September was cited for slow sales of seasonal goods, particularly apparel. However, as cool weather hit the region in early- to mid-October, contacts noted a sharp increase in both store traffic and sales. Inventories, particularly apparel, were generally above plan due to the slower-than-expected sales. Most retailers feel that there is some pent-up demand, however, and there were no plans to increase the use of discounts to clear inventories. Sales of "hard lines," such as home decorations, were reportedly strong while sales of furniture were soft. Retailers remained very optimistic heading into the holiday season with their main concern being finding holiday help.

Housing/construction. Overall construction activity remained robust across most of the region, with a slight pickup in new home construction noted in many areas. Commercial construction remained very strong and one contact reported that commercial contractors were "inundated with work" and were turning down projects. Little has changed in the commercial segment from our last report although one contact in the Indianapolis area noted that the industrial segment in that area may be slightly overbuilt. New home sales and construction benefitted from unseasonably warm weather in the region. Builders, however, noted that the level of traffic through models was down. Most expected traffic to be higher since the economy is so strong and mortgage interest rates so low. However, few expressed concern and most described the market for new

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homes as "healthy." Inventories remained in line with builders' expectations and there were no new reports of incentives or discounts. Most building materials remained readily available--though railway problems were causing some delays in shipments of lumber--and price pressures remained subdued.

Manufacturing. Manufacturing production continued at very high levels in recent weeks while prices for both inputs and outputs remained in check. Production of heavy equipment was reported to be picking up from already high levels and orders remained very strong, particularly for farm equipment. Strength in exports to Canada and Latin America was noted by some industry contacts and there was some improvement in European markets. Inventories of heavy equipment were falling and generally described as low, which would suggest continued high levels of production heading into 1998. Steel plants were also operating at very high levels and most contacts expected the strength to last for the remainder of the year. There was some weakening in the demand for domestic cold-rolled steel due to increased foreign competition. Automakers reported that low inventories of light vehicles were keeping production levels high despite some softening of sales over the last six to eight weeks. For the most part, prices of raw materials to manufacturers remained flat as did output prices. A major producer of wallboard reported that a 6 percent price increase pushed through earlier in the year had been whittled down to 3 percent and continued to be trimmed. Most contacts cited intense competition for manufacturers' inability to raise prices.

Banking/finance. Business lending activity remained strong through September and early October while most bankers indicated that efforts to tighten credit standards on the consumer side continued. The strength on the business side was broad-based with demand for C&I, mergers & acquisitions, and commercial real estate loans showing no signs of subsiding. A contact in one of the District's largest metro areas noted that significant competition was compelling the bank to approve deals that would have been turned down just three months ago. In contrast, another contact in the same metropolitan area stated that business lending standards were being tightened somewhat. Virtually all contacts indicated that caution continued on the consumer side. Mortgage originations were strong and one bank reported a slight pickup in refinancing activity. Banks continued to tighten credit card standards, however, and this was paying off in the form of increased profitability. Asset quality was generally described as very good in the business segment, and good to improving in the consumer segment.

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Labor markets. The District's labor markets continued to tighten and there were a few new reports of intensifying wage pressures. State analysts reported that initial unemployment claims at the beginning of October had reached their lowest level for the period since 1994. Temporary help services were turning to state employment agencies to help fill orders, according to one state analyst. One contact noted that some businesses are "desperately short of people" and manufacturers are most widely cited as having the most difficulty, particularly in filling entry-level positions. Many areas reported that manufacturing employment was picking up, but this is not being reflected in the government's official statistics. Contacts in eastern Wisconsin and central Illinois cited strong job growth in the capital equipment industry, while a Detroit area staffing service noted softening orders from auto suppliers. Many areas were experiencing increases in finance and accounting occupations, with demand broad-based across industry sectors. Retailers in the region were already expressing concerns about finding holiday help and were still finding information and technology workers in short supply. Wage pressures continued to mount in those occupations where the most severe shortages existed and there were new reports of intensifying pressures in rural areas, where labor markets were tightening.

Agriculture. The fall harvest has made excellent progress in District states, aided by ideal weather conditions. The faster-than-normal harvest pace will help to minimize any late-season yield losses. However, it may add to the seasonal glut that often temporarily clogs grain storage and transportation facilities in rural areas at this time of year. The widely-reported railcar problems have the attention of many observers, but as yet have not been much of a factor in District grain markets. Over the years, trucks have handled an increasing share of the local grain hauling requirements.

A surge in grain prices during the first half of October departed from the downtrend that normally extends through the harvest season. The sharp rise reflects some pivotal issues that add to the speculative momentum in the relatively tight world grain markets. The growing focus on El Nino and the uncertain weather implications that might result in food-growing areas of the world is one such issue. Another reflects the uncertainty as to whether China will be a net importer or exporter of feed grains in the year ahead.

EIGHTH DISTRICT - ST. LOUIS

Summary

The District economy continues to operate at a high level, and contacts remain optimistic about future economic prospects. Tightness in labor markets, though, continues to be a concern. Increased sales are prompting plant expansions and employment gains. State sales tax collections through August suggest fairly strong consumer demand for goods and services. Residential construction remains below last year's levels, and demand for apartments appears to be tapering off. Loans outstanding at large District banks rose slightly in the two months ending in September. Favorable harvest conditions prevail throughout most of the District; early reports on yields indicate they are meeting expectations.

Manufacturing and Other Business Activity

Most District contacts report a continued high level of economic activity and optimism. A few have commented that they see economic growth leveling off or slowing slightly from, as one stated, "the aggressive growth patterns of the recent past." Tight labor markets remain a general concern for contacts, who see this as potentially curbing future growth. Some labor shortages are being offset by more sophisticated inventory control systems and computer-based purchasing systems. In one area, a community college plans to open a job-training center that will be a public/private partnership to address the training needs of local businesses.

On the heels of increased sales and plant expansions and development, employment is generally on the rise. A telecommunications firm announced that it will convert an old manufacturing warehouse in the St. Louis region into a telemarketing center that will employ about 1,500 workers. A trust company is opening a regional office in St. Louis to handle some of the new accounts it bought from NationsBank. About 200 employees will be hired, many of

whom previously worked for Boatmen's Trust. A contact in the furniture industry reports that a Canadian firm is relocating to northeast Mississippi, bringing about 200 jobs. A maker of office furniture will open a plant in northeast Arkansas, employing about 250 people.

Layoffs and closings have occurred in some sectors. A shoe manufacturer, noting that two of its domestic plants were no longer economically feasible, is closing these plants and laying off about 300 workers. A regional health management organization has opted to leave the pharmacy benefits management business, eliminating about 150 jobs in the St. Louis region; these services will be outsourced. A contact at a picture frame manufacturer reports that the loss of a major client and a 50 percent drop in projected sales is forcing it to close.

State Tax Receipts

State sales tax data for the District, on balance, indicate moderate to strong growth of consumer spending over the three-month period ending in August. Compared with the same period a year earlier, sales tax growth was most pronounced in Illinois, Missouri and Tennessee, where the year-over-year increases ranged from slightly more than 7 percent to nearly 13 percent.

Real Estate and Construction

Monthly residential construction permits in August picked up in Louisville and Little Rock, remained unchanged in Evansville, Ind., and fell in the District's other nine metropolitan areas. Year-to-date permit levels were up over last year's levels in Jackson, Tenn., and Evansville. They were unchanged in Memphis and below last year's levels in all other metro areas. Several contacts have begun to notice waning demand for apartments, citing shifting demographics as the cause. One contact noted a recent increase in the demand for mobile homes in Kentucky. Nonresidential construction remains relatively strong in the Memphis and St. Louis regions, as well as in parts of western Tennessee.

Banking and Finance

Total loans outstanding on the books of a sample of large District banks rose 0.4 percent in August and September, compared with a 0.3 percent drop in the same two-month period one year ago. Commercial and industrial loans, which rose 2.4 percent, were entirely responsible for the increase, as real estate loans declined 0.1 percent and consumer loans fell 4.9 percent. Loan demand is still reported as strong at smaller District institutions. Bankers at these institutions are concerned, however, about the increasing difficulty in obtaining deposits. Many of them are turning to the fed funds market and the Federal Home Loan Bank System for funding needs.

Agriculture and Natural Resources

Generally favorable harvest conditions prevailed across the Eighth District. Rainfall has caused some disruptions in the Cotton Belt, however, prompting concern about the quality of the crop. Early reports—although decidedly mixed—suggest average to slightly above-average yields for rice. Elsewhere, corn and soybean yields in Missouri, central and southern Illinois and southern Indiana are widely anticipated to be well below last year's levels. Still, scattered reports indicate yields in some corn fields are surprisingly high. It is thought, however, that these high yields are the result of planting typically higher-yielding, early-maturity varieties. Overall, the size of the harvest thus far is consistent with expectations.

Scattered instances of rail disruptions from the Union Pacific logjam have been reported in rural areas. A large Arkansas rice cooperative, for example, reports that a shortage of rail cars has hampered new crop shipments. It is not yet clear whether this problem is of a sufficient magnitude to cause harvest bottlenecks in other areas.

NINTH DISTRICT--MINNEAPOLIS

The Ninth District economy remains strong. Earnings are up, tax receipts exceed expectations, and consumers are willing to spend. Plus, manufacturers report healthy sales, and a boomlet in oil and gas exploration is giving a lift to the North Dakota and Montana economies. To accommodate expanding businesses, builders are scrambling to provide new facilities. Mild fall weather has provided excellent harvest conditions.

The district's robust economy, however, is taxing the ingenuity of employers as they struggle to hire workers in the region's tight labor markets. Although wage increases are not accelerating, employers are increasingly using other financial incentives to lure workers. Firms are holding the line on the prices they pay for nonlabor inputs, but pressures appear to be building for price increases.

General business conditions

A spate of recent reports denotes the continuing strength in the district economy. Strong economies in Minnesota and Wisconsin pushed recent state revenue collections ahead of estimates. Plus, the second quarter earnings of major Minnesota firms were up 12 percent from a year ago. This gain is "another example of why some economists are calling this the strongest economy in 30 years," says the Minnesota state economist.

Consumer spending and tourism

Consumers' willingness to spend manifests the economy's vigor. Recent retail sales have been good in Montana, Wisconsin and Minneapolis/St. Paul, with back to school sales stronger than normal, according to director and advisory council reports. Moreover, two national retailers with headquarters in the district report solid year-to-year sales gains in September.

Meanwhile, tourism spending has recently improved. "We're expecting a strong ending to a slow start," says an Upper Peninsula tourism official about business this fall. Montana tourist-related businesses also experienced a pickup after a slow start.

Manufacturing

Expanding manufacturing sales are also giving the economy a boost. Major Minnesota manufacturers report rising sales and profits, with computer-related producers doing

particularly well. In La Crosse, Wis., manufacturers are pushing on their capacity and having their workers put in considerable overtime, and in North Dakota manufacturing is very robust, according to an advisory council member.

Amid this expansion, restructuring continues. In early October a large South Dakota computer manufacturer announced plans to lay off or reassign 300 workers as part of its ongoing restructuring efforts. Meanwhile, a large Minneapolis/St. Paul manufacturer said it was eliminating 500 jobs in its home and building controls unit.

Construction and real estate

Business is so good that many district firms are running out of room. In Minneapolis/St. Paul industrial space is tight, and in western Wisconsin office space is in short supply. Plus, 60 percent of respondents to a recent survey of Upper Midwest businesses indicate that they are planning expansions during the next year. Thus, across the region new factories, warehouses, office buildings and stores are bursting forth, while home building remains strong.

Natural resource industries

Expanding oil and gas exploration continues to give a boost to the district's western states. North Dakota is experiencing a boomlet, and in Montana more drilling opportunities exist than rigs are available. Low gold prices, however, are curbing mining in Montana.

Agriculture

Mild weather in September and early October is enabling many district farmers to realize their expectations for a banner harvest. In the eastern portion of the district an excellent soybean harvest is nearing completion, and the district's corn crop is maturing and is being harvested faster than normal. "Area farmers thrilled with bumper (spring wheat) crop," heralds a central Montana newspaper. But wheat production in North Dakota is down from a year ago.

Labor markets and prices

"Businesses cry for help," "Help! Say Retailers" and "Temp activity is tempestuous" headline recent newspaper articles discussing the district's intensifying labor shortages.

Helped-wanted advertising at a large South Dakota daily newspaper so far this year is up 30 percent from a year ago, and job turnover is nearing 30 percent at some companies in the Minneapolis/St. Paul area, according to an official with a temporary help firm.

Tight labor markets are spawning creative recruiting efforts. A temporary employment agency is using prized tickets for the Vikings/Green Bay Packers football game to lure new temporary workers. A large Minneapolis/St. Paul retailer has its employees distributing "Wow...great service" cards to employees at other businesses who give them good service. It is intended to "woo" them to the retailer, for on the card is a contact and telephone number for the retailer's human resources department. Firms are also paying bonuses to employees for finding workers.

As the search for workers intensifies, "Employers raise the ante, but not wages," declares another recent newspaper headline. A few firms are offering signing bonuses as high as \$1,000 for new employees who stay with a job for six months; one retailer has expanded the merchandise discounts for its employees; and some employers have begun offering benefits packages to seasonal workers. But a recent survey of Minnesota compensation specialists indicates that over the next 12 months the typical employee will see wages rise about 4 percent, which matches the increases they received during the previous 12 months. Nevertheless, "we have been much more aggressive in paying for talent," states a human resource specialist at a large Minneapolis/St. Paul firm.

Besides striving to hold the line on wage increases, firms are resisting other cost increases. Our company is "not accepting any price increases," reports a purchasing manager for a large Minneapolis/St. Paul company, and "the lid has been on price increases," states another purchasing manager. Nevertheless, about 25 percent of respondents to a recent survey of Upper Midwest businesses report price increases on material inputs.

Moreover, "everyone coming at you wants a price increase," reports one of these purchasing managers, for most firms have not raised prices for the last two to three years. Increasing pressure on firms to maintain profits could push prices up, a Minneapolis/St. Paul manufacturer believes.

TENTH DISTRICT - KANSAS CITY

Overview. The district economy continued to grow moderately the past month, while showing a few signs of easing. Manufacturing activity remained fairly strong. Retail sales edged down, construction activity eased somewhat, and energy activity declined slightly. In the farm economy, record soybean production and average corn production are expected for the current harvest, and ranchers face favorable feeder cattle prices. Labor markets remained tight in much of the district, and reports of rising wages were more common than in previous months. Prices generally held steady at the retail level while increasing slightly for some construction materials.

Retail Sales. Retailers report sales edged down last month and were slightly higher than a year ago. Retailers remain cautiously optimistic that sales will increase over the rest of the year. Most retailers were satisfied with current stocks but expect to expand inventories slightly in the coming months to meet increased demand during the holiday season. Automobile dealers report sales were down slightly last month and lower than a year ago. Sales of light trucks and utility vehicles remained strong, while sales of passenger cars were soft. Dealers have been expanding inventories slightly as they expect sales of new models to increase somewhat the rest of the year.

Manufacturing. Manufacturers operated at moderately high levels of capacity last month. Manufacturing materials were generally available, although problems with rail transportation caused lead times to edge up. Manufacturers have been expanding their inventories slightly but plan to trim inventories somewhat in coming months.

Housing. Builders report housing starts declined slightly last month and were generally unchanged from a year ago. Builders anticipate a normal seasonal slowdown in construction activity toward the end of the year. Sales of new homes were flat last month and were down

slightly from a year ago. Most building materials were readily available and delivery times were normal. Mortgage lenders report some slowing in demand last month but expect little change the rest of the year.

Banking. Bankers report that loans and deposits both edged up last month, leaving loan-deposit ratios unchanged. Commercial and industrial loans, commercial real estate loans, and residential construction loans all increased, while other loan categories were little changed. Demand deposits and MMDAs rose, outweighing a decrease 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. Lending standards were unchanged.

Energy. District energy activity declined slightly last month but remained somewhat stronger than a year ago. Crude oil prices fell while natural gas prices increased, but both oil and gas prices remained well below the peaks reached at the end of last year. The district rig count fell 2 percent in September to a level 17 percent higher than a year ago.

Agriculture. The district corn and soybean harvests are well underway and average yields have been reported. Record plantings should lead to record soybean production in the district, while corn production should be average. Despite good corn and soybean crops, prices may remain at profitable levels due to strong export demand and low stock levels.

Winter wheat planting in the district is almost completed and recent rains have led to favorable growing conditions. Likewise, pasture conditions are expected to be excellent this winter allowing some producers to hold cattle until spring. Nevertheless, the majority of ranchers plan to sell their calves this fall or early next year. With feeder cattle prices well above year-ago

levels, ranchers should recoup some of the losses from the last two years. However, large supplies continue to dampen fed cattle prices. With higher corn prices and the increased cost of feeder cattle, many district feedlots will be unable to make a profit this fall. Nevertheless, projected increases in beef exports could help strengthen fed cattle prices through the remainder of the year.

Wages and Prices. Labor markets remained tight last month in much of the district, with some increased evidence of wage pressures. Retailers report short supplies of part-time and clerical workers, and manufacturers say skilled workers such as welders were hard to find. Somewhat more companies than in past months say they raised wages to attract or retain workers. Prices held steady at the retail level and rose slightly for some construction materials. Retailers expect no major price changes in coming months.

ELEVENTH DISTRICT--DALLAS

In September and early October, Eleventh District economic activity remained at roughly the same level reported in August. Many industries continued to report problems hiring, and some prices were higher. Manufacturing activity was mostly unchanged at a high level. Demand for business services continued to increase strongly, but retail sales growth was slower than expected. Bankers reported little change in lending. Construction activity continued to grow moderately, while energy activity remained extremely strong. Cotton farmers expect an excellent crop, and livestock conditions remained good.

Rail shipping delays caused headaches for some manufacturers, particularly in Houston and for chemicals, steel, lumber, cement and brick. Several firms shifted shipments to trucks and, for the most part, delays have not caused production problems. Stiff competition or long-term contracts are preventing many companies from passing higher shipping costs on to selling prices. Contacts expect the situation to improve by the first quarter of 1998.

Prices. Hiring problems continued to be reported in most industries, and wages were up at some firms. All retailers noted difficulty finding workers and many had increased wages. Many business services firms said sales growth had slowed because they did not have enough labor resources to meet increasing demand. One accounting respondent, for example, said the firm was turning away lower valued business from non-profits and small government entities. Another respondent had recently turned away \$50 million in audit work. Salary increases in the service sector were reported to be larger than earlier this year, and contacts suggest that they are passing along more of this rising cost in higher fees. Electronics firms continued to report that a high percentage of their job openings remain unfilled, but they continue to resist increasing wages to attract more workers because, as one respondent noted, competitive pressures in the industry do not allow wage increases of more than an average of about 3 percent. A shortage of skilled construction workers pushed up their wages.

Several industries reported higher selling prices. Selling prices and rental rates were up for many types of properties, particularly for office space, with year-over-year office rents increasing between 8 percent and double digits in some markets. Energy prices remained higher than expected. Oil prices spent most of August and September between \$19.25 and \$19.75 per barrel, but jumped to near \$22 per barrel on October 3—the highest level since February—as President Clinton dispatched an aircraft carrier to enforce the no-fly zone over southern Iraq. Natural gas prices have been over \$2.30 per Mcf since early August and strengthened by the end of September to over \$3.00. Natural gas inventories have been 3 percent to 4 percent above last year but below normal, and contacts suggest that production is down, especially from the Gulf of Mexico. Petrochemical prices continue to weaken, however, due to large capacity additions both in the U.S. and Asia.

Manufacturing. Manufacturing activity remained mostly unchanged at a high level. Demand for construction-related manufactured products was continued at roughly the same level overall. Demand was up for semiconductors, although declines in memory chip prices have resulted in flattened revenues for several respondents. Demand has increased for low-cost microprocessors due to increased demand for personal computers in the \$1,000 price range. To take advantage of strong margins in late summer, the U.S. refinery system maintained record levels of output in September. The summer driving season seemed reluctant to end, as good weather and a strong economy kept gasoline demand extremely high. Inventories for gasoline are now relatively low. As a by-product, the record levels of gasoline production over the summer led to unusual amounts of heating oil being made. As a result, heating oil inventories are 20 percent above normal for this time of year. Demand for petrochemicals remains very strong.

Services. Demand continued to increase strongly for business services, such as temporary staffing, accounting and legal, and all respondents had a very positive outlook for the coming months. Demand was especially strong for transactions related to mergers, acquisitions and initial public offerings in the energy and high-technology sectors. The transportation industry reports that a strong economy has led to strong demand, particularly for trucking and air cargo.

Retail Sales. Sales growth was slower than expected in September, but picked up some in October. Most contacts were not concerned about the dip in sales growth and remained optimistic about the outlook for future sales. Retailers reported no change in list selling prices, but said that there may be fewer markdowns and less discounting.

Financial Services. Bankers reported little change in lending activity since the last survey. Mortgage lending slowed, seasonally, as expected but remained strong. Contacts said that lower long term rates reduced the spread on consumer and mortgage lending rates, but noted that delinquency rates remain low. Several respondents in the Dallas region mentioned very strong deposit growth year-to-date.

Construction and Real Estate. Construction activity continued to grow moderately. Office construction increased at a strong pace and, while there has been an increase in speculative office construction, most contacts are not yet concerned about overbuilding. Demand for industrial space picked up, but new supply is expected to outpace demand by year-end in some areas of the district, causing a slight drop in occupancy rates. Residential real estate was boosted by stronger than expected demand.

Energy. Demand for oil services and machinery remained extremely strong. Oil-related equipment such as rigs, drill pipe, supply boats, etc, remain in short supply, and prices are rising. People are cited as the biggest constraint on activity. Blue-collar skills such as welders and machinists remain at a premium but also geophysicists and “managerial skills to assess and carry out a project.” Prices for equipment are rising rapidly to levels not seen since the early 1980s, but are still often too low to justify new capacity. Contacts say that the result is no new capacity, and cash flows mostly used for consolidation as competitors buy each other’s capacity.

Agriculture. Cotton farmers expect an excellent crop, and livestock conditions remained good. Farmers and ranchers received much needed rain in early October. Very heavy rains caused flooding, soil erosion and stalled harvest operations in some regions, but helped small grains and winter pastures across the district. Supplemental feeding activity continued, but was decreasing as pastures improved.

TWELFTH DISTRICT--SAN FRANCISCO

Summary

Reports from Beige Book contacts indicate a strong pace of growth in most Twelfth District states in the recent survey period. District retailers reported moderate gains in recent months. Whereas service providers, particularly those in the shipping and freight sector, noted an acceleration in growth above an already rapid trend. Manufacturing activity remained strong in most of the District, as expansions in food-processing and wood product production added to booming growth in aircraft and high-technology equipment manufacturing. Steady demand for residential and non-residential real estate kept construction activity at high level in much of the District. The competition among financial institutions for "good" loans reportedly remained aggressive throughout the District. Respondents' generally positive views of the economy were tempered by many reports of shipping bottlenecks and shortages of both skilled labor and entry-level workers.

Business Sentiment

District respondents expect continued strong performance in the U.S. economy, with regional growth outpacing the national rate. Slightly more than one-half of the respondents expect U.S. GDP growth to remain at or near its long-run average pace, leaving the national rate of unemployment at its current level. An increasing number of respondents expect inflation to edge up in coming quarters. Nearly all respondents expect economic growth in their regions to outpace growth in the national economy over the next year. Respondents are most optimistic about the strength of business investment, housing starts, and foreign trade in their areas.

Retail Trade and Services

Retailers reported moderate growth in retail sales throughout the District. The strongest

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reports were from Nevada and states in the Pacific Northwest, where healthy apparel sales were noted. Contacts in California, Utah and Arizona reported slower retail sales growth than in previous weeks, driven largely by flat food and apparel sales. Despite the slowdown in retail sales, few respondents reported excess inventories or unplanned price cuts. Several respondents reported difficulty finding qualified entry-level workers.

Respondents in the service industry continued to report solid growth. Demand for shipping and freight services in the Pacific Northwest and Intermountain States remained very high. However, capacity constraints in this sector, particularly in rail transportation, could restrain further growth. Travel and tourism remained strong in Utah and California, although fears of “El Nino” reportedly have caused cancellations for the winter tourist season. Several respondents indicated that labor markets for service sector workers remain exceedingly tight at all skill levels. Higher offer wages, signing bonuses, and referral awards were reported for positions ranging from technical sales staff to entry-level bank tellers.

Manufacturing

Manufacturing contacts reported solid gains throughout the Twelfth District, as expansions in food-processing and wood product production augmented ongoing growth in aircraft and high-technology equipment manufacturing. Strong growth in manufacturing reportedly increased capacity utilization rates in recent weeks, especially for manufacturers of paper products, high-tech components, industrial machinery, and aircraft. However, in most sectors, higher utilization rates have not constrained production, with Boeing and its suppliers being the most notable exceptions. In contrast, respondents reported that shipping bottlenecks and labor shortages, particularly for skilled workers, are beginning to limit activity in some areas. Demand for transportation and freight

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services, particularly in the Pacific Northwest, reportedly has outstripped available supply, causing production slowdowns and final product delivery delays in many sectors. Labor shortages reportedly have intensified in recent weeks, and many contacts noted that even when significantly higher wage offers accompany signing bonuses and other benefits, some advertised positions either go unfilled or are filled by workers who lack the desired training.

Agriculture and Resource-related Industries

Reports on agricultural conditions in the District generally were favorable. Good weather conditions have produced better than average harvests in many regions. Increased production of exportable processed food items has boosted demand for many agricultural products. In contrast, concerns over food safety continued to soften the beef market in recent weeks. Harvesting throughout the District reportedly was slowed by shortages of seasonally employed agricultural workers and fierce competition for product transportation from field to market.

Real Estate and Construction

District residential real estate markets remained strong in recent months, despite some slowdown in several states. In the Puget Sound area and parts of Northern and Southern California, heavy demand for single family homes has begun to outpace the available supply of building materials and labor, increasing construction costs and home prices. In parts of southern Arizona, strong demand for retirement residences is keeping construction activity at a high level. In contrast, residential real estate sales in Idaho, Utah, Nevada and Oregon have slowed recently, cooling residential construction activity in these areas.

Commercial real estate and construction activity remains strong in most parts of the District. Respondents reported that commercial office and industrial space has become harder to find, despite

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an acceleration in commercial and industrial construction. In Portland, the first signs of speculative building appeared, as construction began on two downtown office buildings. In California, respondents report declines in commercial vacancy rates throughout the state. Respondents in the hottest markets indicate that the demand for contractors, subcontractors, and materials finally has outpaced supply and is beginning to result in long waits and unbid contracts.

Financial Institutions

District banking conditions remained solid during the recent survey period. Respondents pointed to high liquidity of financial institutions as fueling strong competition among banks to attract quality loan customers. One respondent noted that banks were making an effort to maintain credit standards in the face of decreased demand by quality borrowers.