



**March 3, 2004**

## Summary

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### Summary

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Prepared at the Federal Reserve Bank of Philadelphia based on information collected before February 23, 2004. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a representation of the views of Federal Reserve officials.

Economic activity continued to expand in January and February, according to information received by Federal Reserve District Banks. Growth was variously described as moderate in Boston, Philadelphia, Cleveland, Atlanta, Chicago, St. Louis, and Kansas City, firm in Minneapolis, sound in San Francisco, and showing signs of accelerating in New York, Richmond, and Dallas.

Consumer spending rose in most Districts. There were gains in sales of general merchandise in January and February in all Districts except St. Louis, which reported a slight decline. In contrast to the general improvement in merchandise sales, motor vehicle sales slowed in most Districts. Tourism activity increased compared to last winter. Service sector activity has been expanding. Manufacturing output continued to rise in all Districts except Cleveland, where it has been steady. Real estate market conditions showed little change: commercial markets generally remain soft and demand for housing continues to be strong. Agricultural conditions were mixed: demand for beef appears to be recovering from the effects of mad cow disease but exports of poultry products have been curtailed by the outbreak of avian influenza. Oil and gas production remain at high levels and iron ore processing has increased. Bank lending has been growing moderately.

Employment has been growing slowly in most Federal Reserve Districts. Wages and salaries have increased slightly, but employers report substantial increases for employee health-care costs. Most Reserve Banks reported level or modestly increasing retail prices, but information received from manufacturers and other businesses indicates that commodity prices have moved up more noticeably. The largest increases have been for steel and for lumber and other building materials. Shipping charges have also risen recently.

### Consumer Spending

Retail sales of general merchandise rose in most Federal Reserve Districts in January and February. Strong or strengthening sales were reported in New York, Richmond, and Dallas. Sales growth was moderate in Boston, Philadelphia, Chicago, Minneapolis, Kansas City, and San Francisco. Retailers in Cleveland said sales met or exceeded their expectations. Retail sales in Atlanta moderated slightly in February but remained above the level set in February last year. St. Louis retailers said sales declined slightly relative to a year ago. Spring apparel was said to be selling well in New York, Philadelphia, Cleveland, Richmond, Atlanta, St. Louis, and Kansas City. Sales of electronics, appliances, and home furnishings were relatively strong in Cleveland, Richmond, Atlanta, St. Louis, and Kansas City. Jewelry

was selling well in Atlanta and St. Louis. Reports on retailers' inventories across the 12 Federal Reserve Districts indicated that store stocks were mostly in line with sales. Stores were still receiving spring merchandise, but retailers were generally maintaining conservative inventory plans.

Nearly all Districts reported that auto sales slowed during January and February and compared to a year ago. The exceptions were Boston, where sales picked up in February after falling in January, and Philadelphia, where sales were about steady. Auto dealers in several Districts attributed the falloff in sales to cold or stormy weather that kept shoppers off the lots. With the slowdown in sales, dealers' inventories increased.

Tourism activity has improved. Bountiful snowfalls in mountain areas gave a boost to ski resorts, according to Richmond, Chicago, Minneapolis, Kansas City, and San Francisco. Richmond and Atlanta reported good business at beach resorts, and in New York and San Francisco hotel occupancy increased compared to last year.

### **Services**

Service industry activity moved up in the Districts reporting on this sector. Boston and St. Louis noted increased demand for information technology services. St. Louis also indicated that demand for insurance and health-care services increased, but financial services and transportation activity eased. In the Dallas District, accounting and consulting firms were seeing increased activity compared with the final quarter of last year. In San Francisco, demand has strengthened for media, high-technology, and health-care services. In Richmond service sector business was steady to somewhat improved.

Transportation activity has increased in most parts of the country. National freight companies based in Richmond indicated their business has improved and trucking companies have seen increased activity in Cleveland and Atlanta. Trucking was said to have slowed seasonally in Dallas, but railroads in the Dallas District noted robust activity. Trucking companies reported increased costs for fuel and they said labor costs have increased as a result of recent regulations limiting drivers' hours. Nonetheless, Chicago and Cleveland indicated that sales of heavy trucks have increased.

### **Manufacturing**

Manufacturing activity rose during January and February in 11 of the 12 Federal Reserve Districts. The exception was Cleveland, where factory production rates were said to be steady. There were notable increases for electronic and electrical equipment in Philadelphia, St. Louis, and Dallas, and semiconductors in Boston and San Francisco. Cleveland and Chicago indicated that steel production had increased, and Philadelphia and St. Louis indicated that output of metal products had risen. Production of heavy trucks increased in Chicago, and auto and auto parts production increased in Cleveland and St. Louis, although the increase was said to be seasonal. Atlanta and Dallas noted increased output of lumber, and Richmond and St. Louis reported gains in furniture production. Other manufacturing industries in which expanding activity was noted were biopharmaceuticals (Boston), machine tools (Chicago), aerospace (St. Louis), and chemicals (Cleveland and Chicago). In a few industries reports were mixed. Food processors posted gains in Dallas but declines in St. Louis. Richmond District textile producers were gaining business but there were textile plant closings in the Atlanta District.

### **Real Estate and Construction**

Commercial real estate market conditions have shown little change in most Districts. Continuing high vacancy rates, slowing leasing activity, and downward pressures on rents

were reported by Boston, Philadelphia, Cleveland, Chicago, and Kansas City. Conditions in major commercial real estate markets were mixed in the St. Louis and Minneapolis Districts. Despite the generally slack and unchanged market situation in most parts of the country, a few Districts noted some signs of improvement. In New York and San Francisco vacancies have moved down slightly and rents have begun to recover. Leasing activity has picked up in the Washington, DC area of the Richmond District.

Residential real estate markets continued to be strong in the majority of Districts. Although cold temperatures and winter storms interrupted home building in some areas in January, housing demand generally remained high. Recent gains in home sales and building activity were noted in New York, Philadelphia, Chicago, Dallas, and San Francisco. In Atlanta, St. Louis, Minneapolis, and Kansas City residential real estate activity continued at high levels. In Richmond the housing market was said to have slowed recently, but builders expect activity to pick up. Overall, builders and real estate agents in most Districts expect home sales in 2004 to be close to the 2003 sales record. Home price appreciation was characterized as steady in most Districts with the exception of San Francisco where the rate of increase was said to have slowed somewhat recently.

### **Agriculture**

Agricultural conditions have been mixed. Good citrus crops were reported in the Atlanta and Dallas Districts, although there was some concern in Atlanta that world supplies might exceed demand at current prices. Beef prices were still declining in Chicago and St. Louis while San Francisco reported that they have firmed and Dallas noted that prices and demand had not been affected as much as expected. Chicago reported increased prices for corn, soybeans, and milk. Dry weather in the Kansas City District has adversely affected winter wheat and led some cattle producers to postpone expanding their herds, and ice and snow in the Richmond District has limited grazing there. The outbreak of avian influenza has curtailed exports of poultry from the Philadelphia, Atlanta, and Minneapolis Districts.

### **Natural Resource Industries**

Federal Reserve Districts reporting on the energy sector noted generally strong, steady conditions in January and February. Drilling activity has been fairly level in recent months in the Kansas City and Dallas Districts, but Minneapolis noted a slight decrease in exploration activity. San Francisco indicated that natural gas producers were operating close to full capacity. Rising worldwide demand for steel has stimulated increased iron ore production. Minneapolis reported that iron ore producers in that District were operating at full capacity and ore prices were rising.

### **Financial Services and Credit**

In most Federal Reserve Districts lending by commercial banks grew moderately in January and February. Lending to business firms was rising in Philadelphia, Richmond, Dallas, and San Francisco. In Chicago, lending to small businesses was on the rise while overall business lending was described as flat. Commercial bankers in Richmond and Atlanta said demand for business loans has been restrained as firms are reluctant to increase capital spending. Demand for personal loans, including credit cards, appeared to have eased in New York and Philadelphia, remained steady in Dallas, and increased in Chicago. Mortgage lending declined in Atlanta, Dallas, and San Francisco, and increased slightly in Richmond and Chicago.

Changes in deposits have been mixed. Banks in the Atlanta District have generally had steady growth, but growth has slowed in Cleveland and Dallas where bankers think investors are moving money out of bank deposits and into debt and equity market

instruments. Banks in the Kansas City District indicated that their deposit levels have been steady.

### **Employment and Wages**

Federal Reserve Districts reporting on employment generally noted modest increases in January and February. Boston indicated that temporary help agencies were placing more workers in manufacturing, software development, and government. There has been increased demand for temporary help workers in customer service and sales positions in the Richmond District, in office and health-care jobs in the Dallas District, and for a variety of jobs in the Chicago District. Employment agencies in New York indicated that they have been experiencing gradual increases in demand, and professional employment agencies in the Washington, DC area of the Richmond District have boosted their own staffs in response to increased business from their clients. San Francisco District employers in the retail, construction, and agricultural sectors have been increasing their hiring moderately.

Reports on wages indicated that increases continue to be moderate. However, the rate of increase in benefit costs continues to exceed that of wages. Medical insurance and workers' compensation insurance fees remain on the rise in most Districts, although the rate of increase does not appear to be accelerating.

### **Prices**

Most Reserve Banks reported fairly stable or slowly rising retail prices in January and February, but accelerating increases in some industrial commodity prices. Steel prices have increased, and prices of iron ore and scrap metals have risen as well. Prices of lumber and other materials used in home building were on the rise in most Districts. Energy prices, especially natural gas, remained high in most Districts and Atlanta noted price increases for petrochemicals. Cleveland noted rising rates for shipping by truck and Chicago reported rising costs for overseas shipping, primarily due to increased costs for ocean transport.

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