



January 19, 2005

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Summary

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Prepared at the Federal Reserve Bank of Richmond and based on information collected before January 10, 2005. 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.

Reports from the twelve Federal Reserve districts indicated that economic activity continued to expand from late November through early January. Eleven districts characterized activity as expanding with Atlanta, New York, and Richmond noting that the pace of activity had quickened since their last reports. The Cleveland District was less upbeat, characterizing economic activity in that district as mixed.

Consumer spending was generally higher since the last Beige Book and a number of districts reported that retail sales during the holidays were above year-ago levels. While the pace of spending was sluggish in a number of districts at the beginning of the period, it picked up appreciably by late December. Adding to the strength in household spending was an increase in tourism in several districts. Most districts reported that manufacturing activity firmed and many districts said that businesses planned to increase capital spending in 2005. Although several reports noted some slowing in residential real estate and construction activity, real estate markets remained generally strong. In the financial sector, lending activity was mixed, as modestly higher commercial and industrial lending was tempered by slower residential mortgage lending. Several districts noted that agricultural conditions were favorable and that activity in the energy sector remained strong. Labor markets firmed in a number of districts, but wage pressures generally remained modest. Several districts reported higher prices for building materials and manufacturing inputs, but most reported steady or only slightly higher overall price levels.

Consumer Spending and Tourism

Consumer spending increased in most districts since the last Beige Book report, with only Cleveland, Dallas, and New York reporting that sales were mixed. Boston, Chicago, Dallas, New York, Richmond, and San Francisco said that retail sales were slow in early December but picked up the pace from Christmas through the end of the year. Sales of luxury goods were strong in the Kansas City, Philadelphia, and San Francisco districts, while retailers in the Atlanta, Chicago, and Kansas City districts reported that electronics and jewelry sold well during the holiday season. Boston, Richmond, and San Francisco reported higher sales of building supplies, and Boston, Chicago, and St. Louis noted stronger sales of apparel. Gift cards sold briskly according to the Chicago, Kansas City, Minneapolis, and New York reports. Post-holiday retail inventories were at satisfactory levels in the Kansas City, New York, Philadelphia, and San Francisco districts.

Automobile sales were mixed. Atlanta, Chicago, Cleveland, and Kansas City noted higher sales, but St. Louis and Dallas said new car sales slowed. Atlanta, Philadelphia, and San Francisco noted that sales of foreign cars outperformed domestic makes. Dealers in the Chicago, Dallas, and Philadelphia districts reported that automobile dealers' inventories remained above desired levels.

Tourist activity strengthened in several districts. Boston said that increased business travel, corporate spending, citywide conventions and increased international travel boosted hotel occupancy rates. Occupancy rates were also up in the San Francisco district, and the number of Japanese visitors to Hawaii has returned to pre-September 11 levels. New York noted that tourist activity was higher both upstate and in New York City where Broadway theaters set a box-office record during the last week of the year. In addition, the Atlanta report indicated that tourism was strong and that central Florida theme parks were filled to capacity. Kansas City indicated that some ski resorts in the district reported near-record levels of visitors. Richmond reported that because of unseasonably mild weather, hotels were booked to capacity in coastal areas and that some were turning tourists away during the week after Christmas.

Services

The Dallas, New York, Philadelphia, San Francisco, and St. Louis districts reported steady to stronger demand at services firms since the last Beige Book. Atlanta, Dallas, San Francisco, and St. Louis noted stronger demand for transportation services, with some seaports in the Atlanta district posting double-digit gains in both inbound and outbound shipping. Air passenger traffic was higher at airports in the Chicago, Dallas, Kansas City, and New York districts while air freight volume increased in the Atlanta district. New York's report also noted that the securities industry ended 2004 on a strong note.

Manufacturing

Manufacturing activity strengthened since the last Beige Book report. Nine of the 12 districts indicated that factory output rose, while Chicago, Cleveland, and Richmond noted that production was steady. Boston, Philadelphia, and San Francisco indicated that demand for transportation equipment strengthened measurably. Production of electrical machinery increased in the Philadelphia district, and Chicago reported strong output of heavy equipment. Atlanta, Dallas, and San Francisco reported that production of building materials picked up, while Chicago and San Francisco indicated that orders for machine tools increased in their districts. San Francisco also reported that semiconductor orders and sales were generally solid.

But some manufacturing sectors weakened. Richmond reported that textiles and apparel shipments continued to decline. Atlanta reported layoffs at a computer circuit board plant, and Dallas noted slowing demand in consumer communications equipment. Philadelphia indicated that demand softened for lumber and wood products, paper products, and plastics, and Cleveland reported that sales at automobile industry suppliers slowed at year-end. St. Louis said that firms in the fabricated metal product, wood product, chemical, and apparel industries announced plant closings and layoffs.

Looking ahead, manufacturers expected conditions to remain positive in coming months. Most districts reported that manufacturers intend to increase their capital spending in 2005. Firms in the Chicago district upped their planned capital expenditures for next year; most have already begun to place orders to accomplish those spending goals. Minneapolis indicated that expectations of higher sales by businesses led to plans to increase capital spending in 2005. Kansas City noted greater capital spending in 2005 to replace outdated

equipment. Richmond reported that manufacturers planned to increase capital spending despite their skepticism about the sustainability of the U.S. economic recovery.

Construction and Real Estate

Residential real estate activity generally remained strong. Atlanta, Boston, New York, Richmond, and San Francisco said that housing markets in their districts continued to show strength in the fourth quarter of 2004, and Dallas and St. Louis reported some improvement since the last Beige Book. Chicago reported mixed housing activity, possibly because of a seasonal slowdown in December, but noted a slight pickup in sales during the first week of January; real estate activity was also mixed in the Minneapolis district. The Kansas City District reported flat to slightly higher home sales compared with a year earlier. New York reported that prices for upper-end New Jersey properties leveled off, or pulled back, but that prices for Manhattan co-ops and condos continued to rise. Richmond said home prices continued to rise in most areas of that district.

Commercial real estate conditions strengthened in most districts in December and early January. Real estate agents in the Dallas, New York, Richmond, San Francisco, and St. Louis districts reported that leasing activity increased--particularly for office space. Office leasing was especially brisk in Washington, D.C., and New York City, two of the nation's strongest commercial markets. Contacts in New York said the recent uptick in activity sent the Class A office vacancy rate to a two-and-a-half-year low and may be a signal of increased hiring in that area. In other districts, vacancies were mixed--rates dipped in San Francisco, St. Louis, and most of the Kansas City District, but were generally unchanged in other areas. Adding to the positive tone, commercial construction activity was higher since the last Beige Book report--contacts in Atlanta, Chicago, Minnesota, Richmond, and St. Louis reported new industrial or office construction activity, while retail construction maintained a generally steady pace.

Banking and Finance

Lending activity remained generally mixed as slower residential mortgage lending offset somewhat higher commercial and industrial lending in many districts. Commercial lending was modestly higher in the Atlanta, Chicago, and San Francisco districts while commercial and industrial lending was stronger in the Kansas City, Philadelphia, and St. Louis districts. Residential mortgage lending, however, declined in the Chicago, Dallas, and New York districts.

Several districts reported that credit conditions were steady, though Dallas added that competition between banks in that district could threaten credit quality in the months ahead. In addition, Chicago and San Francisco reported that banks' profit margins on loans were thin.

Agriculture and Natural Resources

Several districts noted that crop and livestock conditions were generally favorable, despite widely varying weather conditions. Richmond indicated that unseasonably warm weather in early December accelerated the development of winter grains and extended the grazing period for livestock. But very cold temperatures and snowfall in late December led to supplemental feeding of livestock. A major snow storm affected part of the St. Louis District in late December, leaving fields and pastures muddy. Despite the excess soil moisture, St. Louis said the winter wheat crop was in mostly fair to good condition. Minneapolis noted that Montana's 2005 winter wheat crop was good to excellent despite little snow cover to protect against freeze or wind damage. Kansas City added that some producers in the western part of its district remained concerned that dry pastures could deteriorate further.

Agricultural prices were generally higher. The Chicago district reported that net farm income jumped last year as a result of profitable livestock operations and record corn and soybean harvests, much of which was forward-contracted at unusually high prices. In addition, Minneapolis reported milk prices were higher.

Activity in the energy industry remained strong according to reports from the Dallas, Kansas City, Minneapolis, and San Francisco districts. Minneapolis indicated increased mining activity, noting that the delivery of some mining machinery required two-year waits. Kansas City reported that oil and gas drilling rig counts remained well above year-ago levels, and noted constraints on drilling due to labor and equipment shortages. Dallas added that the level of land drilling was mostly unchanged but that offshore activity had picked up.

Labor Markets

Districts generally reported firmer labor markets in late 2004. Contacts in Dallas, Kansas City, Minneapolis, New York, and Richmond reported improvement on the job front, while respondents in Boston, Chicago, and San Francisco saw little change in hiring activity.

Manufacturing employment rose in Kansas City, New York, Richmond and St. Louis, while factory owners in Philadelphia anticipated adding workers in coming months. Planned factory hiring in Cleveland was mixed by product type--producers of nondurable goods predicted little change in future hiring, but makers of durable goods anticipated adding to their payrolls in the months ahead. Services sector respondents in Dallas, Richmond, and St. Louis reported broad-based strengthening in services sector employment, and contacts in New York and Philadelphia noted a particularly strong pickup in securities industry hiring.

Information on employment staffing services firms was mostly positive, but varied by district. Contacts in Cleveland, New York, Philadelphia, and St. Louis reported a moderate to brisk rise in demand, but Richmond noted generally flat activity and Dallas reported a softening in demand for temporary workers. Chicago also experienced a modest decline, but attributed it to a normal seasonal lull.

The reports from Kansas City, Minneapolis, and San Francisco indicated that wage increases generally continued to be modest. However, Cleveland noted that in response to the strong pickup in shipping demand, trucking firms have been attempting to expand their workforce by raising their wage rates and offering nonpecuniary incentives. Kansas City also noted higher wages for skilled factory workers in short supply, while Richmond noted that wage increases picked up in the services sector.

Prices

Inflationary pressures remained largely in check in December and early January. While many manufacturers and builders continued to report small increases in input costs, price increases for final goods and services were generally modest.

In manufacturing, input prices rose modestly in most districts, but Boston and Minneapolis reported that some input prices rose sharply. Manufacturers of nondurable goods in the Cleveland district noted that prices for raw materials continued to rise, while prices for durable goods inputs were steady. Prices charged by manufacturers increased modestly in Kansas City, New York, and Richmond, and remained in check in Atlanta and Chicago. Increases in the costs of building materials were mixed by district. Modest to sharp price hikes were widely reported in Atlanta, Kansas City, and Minneapolis, but material prices were flat in Cleveland and New York, and eased somewhat in San Francisco.

Overall, price inflation remained relatively steady in recent weeks. Reports from Atlanta, Boston, Chicago, Kansas City, New York, Richmond, and San Francisco reported that price increases remained largely in check. Contacts in Dallas noted that many firms were unable to pass rising costs along to the customer due to stiff competition, and Chicago noted that competition in the retail sector is expected to limit price increases.

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