



April 20, 2005

Summary

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Summary

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Prepared at the Federal Reserve Bank of Boston and based on information collected on or before April 11, 2005. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Reports from all twelve Federal Reserve Districts indicate that business activity continued to expand from late February through early April. Kansas City and San Francisco noted solid growth, Chicago and Dallas characterized growth as moderate, and Atlanta reported a robust pace. By contrast, while citing positive growth, New York and Cleveland mentioned uneven progress across sectors, and Richmond stated that signs of improvement in April followed a restrained March.

More than one-half of the Districts reported that retail activity was up, from modestly to strongly. Among the remaining Districts, Chicago said consumer spending was subdued, Dallas noted that retailers were disappointed with recent growth, and Cleveland reported some deterioration after improvement earlier in the year. Tourism was generally doing well in those Districts that mentioned it.

Districts described manufacturing activity as ahead of year-earlier or previously-reported levels, with reports ranging from "rising briskly" in the Kansas City District to "continuing at solid levels" for contacts around Chicago. Information on service industries was generally positive. Residential real estate markets remained strong across most of the country, while commercial real estate conditions varied. Price pressures have intensified in a number of Districts, and most report that high or rising energy prices are a concern across sectors.

Consumer Spending and Tourism

The majority of Districts experienced improving retail sales overall, but several showed flat or disappointing results. In Minneapolis, contacts indicated that retail sales increased between 5 percent and 12 percent over the previous year. St. Louis also reported strong growth, with Boston, Philadelphia, Atlanta, Kansas City, and San Francisco recording modest to solid gains. Among the remaining five Districts, New York, Chicago, and Dallas characterized consumer spending growth as either subdued or disappointing, while Cleveland and Richmond cited mixed trends during the reporting period. Contacts in these five Districts attributed sluggish spending in part to unfavorable weather conditions, and in part to high or rising energy and gasoline prices. Retail selling prices were described as reasonably stable to date, although some contacts cited evidence of increased prices and pricing power.

New vehicle sales were flat or slightly up in most of the Districts reporting on this category. The exceptions were San Francisco, which reported strong sales, and Dallas, where car sales were weaker than a year ago. Contacts in several Districts also mentioned softening demand for domestic vehicles, especially trucks and SUVs, although most dealers in the Richmond

District said they had not seen a shift to smaller cars despite higher gasoline prices. In other product categories, apparel and jewelry sales were strong in many regions.

Spending on travel and tourism improved throughout much of the country. New York and San Francisco reported brisk activity compared with a year ago, citing rising occupancy rates and higher revenues per room. Bolstered by foreign visitors, Florida recorded high passenger counts on cruise lines and robust bookings at theme parks. Boston, Philadelphia, and Kansas City also reported stronger tourist-related growth. Weather was an important factor in the Richmond, Chicago, and Minneapolis Districts, as areas with favorable winter weather enjoyed increased business while those with bad weather saw flat or sluggish growth.

Service Industries

In general, firms in the service sector enjoyed a moderate increase in activity. St. Louis reported expansion in most areas, and San Francisco noted solid demand growth, especially in health-care, transportation, and food services. According to Atlanta, temporary employee hiring maintained a brisk pace, while Philadelphia, Cleveland, and Richmond observed some pickup in demand at employment agencies. By contrast, Chicago and Dallas indicated more modest growth at temporary staffing firms. Demand for trucking and shipping services in several Districts reportedly eased somewhat as firms began passing on higher fuel costs to customers. However, Philadelphia reported increased trucking activity despite higher freight rates. Dallas cited strong conditions in the accounting industry, while business at law firms remained unchanged. Boston identified robust demand at both advertising and management consulting firms.

Manufacturing

The updates on manufacturing were largely positive. Eleven of the twelve Districts indicated that production or orders were rising, while Chicago characterized activity as continuing at solid levels with the exception of continued weakness in light vehicle production. Several Districts with largely upbeat reports nevertheless indicated that increases in manufacturing output may be moderating a little. For example, New York cited a "loss of momentum" in the manufacturing sector, and Cleveland stated that "many firms noted flattening new orders growth" for durable goods.

Districts reported strong or rising demand for various durable goods, including building materials, machinery and machine tools, fabricated metals, energy-related equipment, and defense equipment. Shortages of tires and metal parts were said to be constraining heavy truck and other production in Chicago, Minneapolis, St. Louis, and Kansas City.

Manufacturers in all Districts were reportedly facing rising costs for a variety of inputs, most notably energy, transportation, petrochemicals, and other petroleum-based products. Moreover, according to Dallas, expansions of petrochemical capacity are not expected to provide price relief for at least another year. On the other hand, several Districts mentioned that steel prices were stabilizing, albeit at high levels, and Philadelphia's survey revealed that the number of companies saying prices had risen in March was lower than it had been during the fall and early winter.

Overall, manufacturers' output prices appear to be rising modestly. Most Districts found that firms were having partial success passing on higher energy and materials costs to their customers. However, several cited instances of firms having to rescind price increases and accept lower margins. Reduced margins remained the norm in the Cleveland District, and rising energy costs were specified as a source of "concern" or "caution" among manufacturers in New York, St. Louis, and Dallas.

Labor demand in the manufacturing sector appears to be mixed, with some Districts placing more emphasis on additions to employment and others on cutbacks. District reports on capital spending tended to be moderately positive. Kansas City referred to "solid growth" in capital investment, and Philadelphia took note of the fact that very few companies expect to reduce their capital spending in the coming six months. Nevertheless, Boston described manufacturers as "closely managing" their capital expenditures.

Real Estate and Construction

Residential real estate markets were very active during March and early April, with Districts noting increased activity levels compared with the previous report. Demand for houses was strong and residential sales were high in three-quarters of the Districts. New York, Richmond, and Atlanta cited low housing inventories, while Boston mentioned increased time on the market for high-priced homes. Several Districts indicated that home prices rose. Reports on new housing construction were more mixed. Atlanta, Minneapolis, Kansas City, and San Francisco said the pace of home construction was strong or picking up, but St. Louis and Dallas noted slower residential construction.

Commercial real estate markets varied. Office vacancy rates declined in New York, Richmond, St. Louis, Minneapolis, and San Francisco. New commercial construction was robust in Cleveland, Atlanta, St. Louis, Dallas and San Francisco, but slow in Richmond. Chicago reported steady vacancy and rental rates.

Banking and Finance

For most Districts reporting on financial services, demand for loans increased across a range of categories. Almost all Districts mentioned increases in commercial lending activity, and Philadelphia, St. Louis, Kansas City, and San Francisco noted industrial lending as an area of strength. The Cleveland District cited increased demand for loans to the manufacturing industry, specifically. Reports on demand for mortgages were mixed, and the New York, Chicago, and Kansas City Districts noted weakness in refinancing activity. Demand for non-bank financial services was disappointing, with New York reporting a recent slowing in the securities industry, and investment companies from the Philadelphia District noting general caution on the part of investors.

Other banking indicators were holding steady or improving in some cases. Philadelphia and Kansas City reported growth in deposits, while Cleveland cited rising core deposits at larger banks. Credit conditions and delinquency rates have improved according to the New York, Chicago, and San Francisco Districts, and held roughly the same in the Dallas and Chicago Districts.

Agriculture and Natural Resources

Planting activities are under way in the agricultural Districts, which generally reported good spring conditions. By exception, wet weather has caused delays in parts of the Richmond and Atlanta Districts, while drought conditions continued or worsened in parts of the Minneapolis and Kansas City Districts. Still, contacts indicated that the winter wheat and other crops are generally in good shape, as are range land, pasturage, and livestock. However, canker disease required destruction of part of the Florida citrus crop. In addition, growers in the Chicago, St. Louis, and Minneapolis Districts are cutting planned soybean acreage, reflecting some concern about soybean rust. Chicago, Kansas City, and San Francisco contacts noted that fuel, fertilizer, and other input costs are rising. Chicago bankers voiced concern that higher rents and interest rates could adversely affect cash flow at large farming operations. Atlanta contacts reported strong export demand for cotton and poultry, while Dallas noted improved selling prices for wheat, corn, and soybeans and favorable prices for livestock.

Minneapolis, Kansas City and Dallas reported that activity in the energy sector is revving up. According to contacts in Dallas, the U.S. rig count is at the highest level since 1986, and drilling plans are increasing faster than predicted earlier this year. Kansas City respondents noted that shortages of labor and equipment are keeping drilling activity slightly below desired levels at some firms, while some Dallas contacts say they are thinking of adding capacity. In San Francisco, drilling costs are rising. Dallas contacts report that producers are turning their attention to coal-bed methane, tight gas, tar sands, and gas shale, while service companies seek to create new products to support the development of unconventional resources. In the Minneapolis District, a large-scale wind energy project is planned for Montana. Mining activity is also on the rise, with output stable or growing at Montana's iron, palladium/platinum, and copper mines.

Prices and Wages

Reports from many Districts suggested that upward price pressures have strengthened, although actual increases to date in vendor prices and selling prices have generally remained moderate. Much of the pressure derives from energy costs, although contacts cited the lower dollar and rising costs of building materials as well. Most Districts said manufacturers, retailers, or services firms were able to pass at least a portion of cost increases along to their customers. However, only Chicago and Dallas suggested that some contacts have raised prices enough to increase margins or profits.

In two-thirds of the Districts, retail or tourism contacts expressed concern that high energy prices were already, or could soon be, damping consumer demand. Distribution (shipping, trucking, freight, delivery) firms and utilities shared similar apprehensions, having imposed fuel surcharges in many cases, according to Cleveland, Richmond, Chicago, and Minneapolis. As noted above, manufacturers also mentioned rising energy costs. San Francisco stated that increasing costs have prompted manufacturers to "keep production as close as possible to demand," and Dallas indicated that uncertainty about energy prices has added caution to the outlook for business activity.

Boston, Richmond, Chicago, Minneapolis, and Kansas City reported modest or moderate wage increases in various sectors, as labor markets in a few areas or occupations became somewhat tighter. By contrast, Cleveland cited stable wages in trucking, and Dallas said its contacts saw little or no wage pressure. Atlanta, Chicago, Dallas, and San Francisco indicated that benefits costs, especially health care, continue to rise.

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