



January 18, 2006

Summary

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Summary

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Prepared at the Federal Reserve Bank of Cleveland and based on information collected before January 9, 2006. 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.

Economic expansion continued across the twelve Federal Reserve Districts through the last several weeks of 2005. Six--New York, Philadelphia, Chicago, St. Louis, Minneapolis, and Kansas City--characterized their economies as expanding moderately or modestly. Activity accelerated or increased at a solid pace in the San Francisco, Richmond, Atlanta, and Dallas Districts. Boston characterized activity as continuing to expand, while Cleveland reported that conditions remained reasonably strong.

Most Districts reported moderate increases in employment. Labor markets tightened in some areas and for some occupations, but on the whole, wage increases were characterized as moderate. Contacts reported that input-price pressures have continued for many items, particularly early in the supply chain, but they were less intense at year-end than earlier. Retail prices and producers' prices for more finished goods, however, were widely reported as rising only moderately or remaining stable.

Retail sales rose in most Districts, and those Districts that reported on travel and tourism spending said it was generally strong. Increases in manufacturing activity were widely reported. Most Districts indicated some cooling in residential real estate activity, while many noted that commercial real estate activity generally continued to improve. Consumer borrowing was flat or fell in most Districts, while commercial borrowing was more mixed, with many Districts reporting moderate increases in activity. Conditions in the energy sector seemed strong, while agricultural activity was mixed.

Prices

Several Districts (San Francisco, Kansas City, Chicago, Richmond, Cleveland, Philadelphia, and Boston) reported that increases in energy prices moderated, or actually fell, albeit from high levels. In the San Francisco, Cleveland, and Richmond Districts, these developments were thought to be associated with a wider easing in overall price pressures. However, in the remaining nine Districts, nonlabor-input-cost increases continued to concern companies, particularly those in the manufacturing sector. Producers were reported to have attempted to recoup these costs, although, according to the Atlanta, Boston, San Francisco, and Dallas Districts, intense competition was thought to be holding down price increases in parts of the supply chain further "downstream." Increases in the prices of construction materials were widely reported.

Retail prices were generally regarded as stable, though there was some significant discounting reported in the Cleveland and Atlanta Districts during the holiday selling season.

More moderate discounting was reported in the Dallas District, levels about the same as last year were reported in the San Francisco District, and no widespread discounting was reported in the Philadelphia District. Price increases are planned in the months ahead by a large share of retailers, according to the Kansas City District.

Employment and Wages

Most Districts reported signs of continued, if generally moderate, increases in employment. Cleveland, Minneapolis, and Richmond all cited moderate employment gains, with Richmond noting that its rate represented a slowdown. New York, Atlanta, Kansas City, and Dallas reported evidence of stronger employment growth. However, Boston noted that output growth had generally not translated into higher employment, while St. Louis reported a widely mixed pattern of layoffs and hiring. Hiring at financial and legal services firms is boosting the New York District's employment growth, although New York also reported some hiring in manufacturing. Atlanta reported strong demand for both skilled and unskilled labor, in part boosted by storm-recovery efforts.

Atlanta reported several locations with tight labor market conditions, while Boston, New York, Philadelphia, Chicago, Kansas City, Dallas, and San Francisco all reported specific occupations in which jobs have been difficult to fill. Several of these Districts cited trucking jobs. Skilled construction workers are relatively sought after in Dallas and San Francisco, and skilled manufacturing jobs were mentioned by Boston, Chicago, and Dallas. Atlanta listed a variety of specialties in "extreme shortage." New York and San Francisco noted that finance-industry labor markets were relatively tight. Despite reports of labor market tightness, Boston, Philadelphia, Minneapolis, Kansas City, and San Francisco all noted that wage increases have been generally moderate. However, New York, Chicago, and Dallas all reported some acceleration in compensation.

Consumer Spending

All Districts reported that their retail sales rose during this latest holiday selling season except Cleveland, where sales were generally flat or less than at this time a year ago. Philadelphia, Chicago, St. Louis, Minneapolis, and Kansas City reported modest to moderate increases. Boston, New York, Richmond, Atlanta, Dallas, and San Francisco reported stronger holiday sales than these Districts. The Cleveland, Richmond, Chicago, Minneapolis, and Dallas Districts noted significant increases in gift card sales, which led retailers in Richmond and Dallas to anticipate stronger sales and profits in early 2006. Most merchants appear to have carefully controlled their inventories, which are generally at desired levels.

Automobile sales were generally somewhat sluggish across the nation. Dealers fared best in the Richmond, San Francisco, and Dallas Districts, where sales improved from low levels. Sales trends were somewhat more mixed in the Chicago and Atlanta Districts. Atlanta and Philadelphia reported that sales remained strong for foreign brands, even as demand waned for domestic ones, sales of which were reportedly not helped much by manufacturers' promotions. Philadelphia and Kansas City characterized truck and SUV sales as especially slow.

Travel and Tourism

Travel and tourism remained robust across most of the country. The San Francisco District reported that travel and tourism spending in Hawaii toward the end of the year occurred at a record-setting pace. Elsewhere, ski resorts throughout the Kansas City and Minnesota Districts have done well this winter, though a few areas have suffered from a lack of snow. In the Southeast, the Atlanta and Richmond Districts also reported robust activity, some of which was thought to be the result of unusually warm weather. Tourist activity appeared to be

recovering somewhat in hurricane-affected areas. Finally, in the Northeast, travel and tourism remained strong.

Manufacturing

Increases in manufacturing activity were widely reported across the country. Only the St. Louis District characterized industrial activity as mixed. Elsewhere, robust expansion was reported in the San Francisco, Dallas, Kansas City, Minnesota, Chicago, New York, and Boston Districts. More moderate expansion was indicated in the Cleveland, Richmond, Philadelphia, and Atlanta Districts.

Production of high-technology goods was steady to slightly increasing toward the end of 2005, according to the San Francisco and Dallas Districts. And defense and aerospace industry production improved in the San Francisco, Boston, and Atlanta Districts.

Manufacturers of machine tools and industrial equipment also reported more robust demand in the San Francisco, Chicago, and Philadelphia Districts. Production of construction-related materials and equipment expanded noticeably in the San Francisco, Dallas, Chicago, and St. Louis Districts but was characterized as slightly less strong in the Boston District. Primary metals producers reported strong demand in the Cleveland, Chicago, and Dallas Districts. Producers of plastics and petrochemicals noted some slowing in demand in the Philadelphia and Dallas Districts, though this was from fairly high levels. By contrast, reports from the Richmond and St. Louis Districts suggested some improvement in the sector. And weakness in the textile industry was reported in the Boston, Richmond, and Atlanta Districts.

In the transportation equipment sector, reports from the Boston, Philadelphia, and Atlanta Districts suggested weakness among automakers and their suppliers. However, in the Cleveland and Chicago Districts, activity appeared to be somewhat stronger. Heavy truck production was also characterized as improving in the Chicago District. Conditions in the transportation equipment sector were more mixed in the St. Louis District.

Trucking and Shipping

Trucking and shipping demand remained strong across the country, but companies were constrained by continuing driver shortages in the Atlanta, Cleveland, Chicago, and Philadelphia Districts. In addition, despite the ongoing use of fuel surcharges, contacts in Cleveland, Dallas, and Atlanta noted that margins tightened because of fuel-cost increases. Cleveland and Dallas reported plans for increased capital spending in the trucking industry. Dallas also reported that both railroads and airlines saw rising demand.

Construction and Real Estate

Many Districts reported moderation in residential real estate activity, although from a high level. Boston, New York, Cleveland, Richmond, Atlanta, Chicago, and Minneapolis reported some cooling in real estate markets. While some of the hottest markets in the San Francisco District have cooled--for example, Southern California and the San Francisco Bay Area--other areas, such as Oregon and especially Hawaii, have reportedly heated up further. Kansas City and Dallas continued to see strong housing markets. And construction and repair work remained brisk in Louisiana and Mississippi.

Conditions in Districts' commercial real estate markets generally continued to improve. Vacancy rates fell in the San Francisco, Minneapolis, New York, Dallas, Richmond, and Kansas City Districts. Chicago reported a more mixed picture, with some areas of the District expanding but activity in the city of Chicago flat. Largely because of lower vacancy rates, rents rose in San Francisco and New York, while previous concessions were reduced or eliminated in Dallas. New construction activity was reported to be increasing in the San

Francisco, Minneapolis, St. Louis, Atlanta, and Cleveland Districts, and many contacts expect this trend to continue in 2006.

Banking and Finance

The Cleveland, Kansas City, Philadelphia, San Francisco, and St. Louis Districts saw moderate increases in commercial lending activity, while Chicago and Richmond reported that activity had slowed and Atlanta reported that activity was mixed. Consumer lending was flat or fell slightly in the Atlanta, Chicago, Cleveland, Kansas City, New York, Richmond, St. Louis, and San Francisco Districts. The Philadelphia District was an exception, noting gains in consumer and residential real estate loans, but contacts noted that they expected lending for residential real estate to experience modest declines in the future. In the Dallas District, deposit growth was strong, while Cleveland, Kansas City, and St. Louis reported modest increases in total deposits. New York reported that conditions in the securities industry remained robust, with employees receiving significant increases in bonuses this year.

Energy and Natural Resources

Conditions in the energy sector were characterized as strong or stable at a high level by four of the five Districts reporting on natural resources. As a result, San Francisco, Dallas, and Kansas City all reported shortages of labor, materials, and equipment among energy-related enterprises. Producers of natural gas and oil reportedly operated near 100 percent capacity in the San Francisco District, while the Atlanta and Dallas Districts reported that facilities in the Gulf of Mexico continued to recover from hurricane-related damage. Minneapolis reported that most mining operations in its District were running near capacity.

Agriculture

Dallas, Kansas City, St. Louis, and Chicago all reported that low levels of precipitation were affecting crops and have the potential to lower yields in the spring, while Richmond reported that cold weather and abundant precipitation slowed harvesting activity in November and December. Citrus producers in the Atlanta and Dallas Districts reported a boost in profits from an increase in prices in the wake of substantial hurricane damage to the citrus crop in Florida. Livestock reports were mixed, with San Francisco reporting increases in sales, Chicago reporting rising cattle prices and stable hog prices, and Dallas and Kansas City reporting reductions or anticipated reductions in herd sizes.

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