

FEDERAL RESERVE BANK OF SAN FRANCISCO

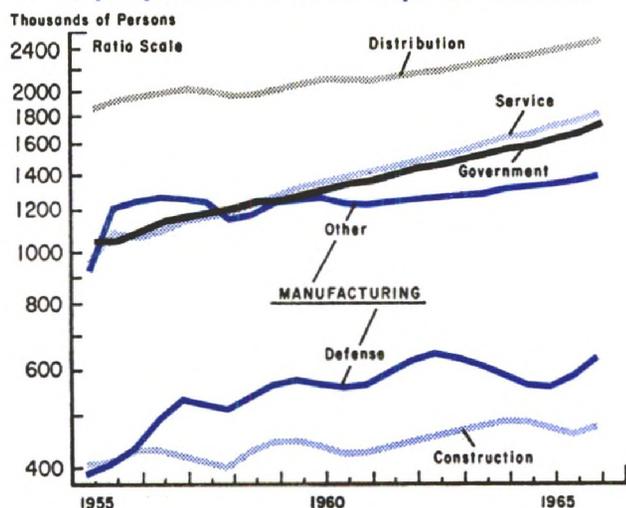
Regional Balance

THE West followed the national pattern during the second quarter: its economy continued to boom, but at a less startling pace than earlier in the year. Total employment in Twelfth District states increased by 1.2 percent during the April-June period, as against a 1.7-percent increase in the preceding quarter, as practically all industries reported continued employment gains.

In the year to date, regional business activity has advanced at a well-balanced pace. Almost all major sectors have expanded employment by about 3 percent over the late-1965 level—the obvious exception being aerospace manufacturing, with a 10-percent increase. Even construction, despite the severe slump in housing, has recorded a gain in employment because of the boom in industrial, commercial, and public building.

The regional boom has brightened the unemployment picture, too. California's unemployment rate remained high, near the 5-percent level, during the first half of 1966, but this figure was far below the average 6-percent rate of the 1964-65 period. The rest of the District, because of the exuberance of the Northwest business scene, boasted a 3.5-percent jobless rate in the January-June period,

All sectors exhibit gains in employment . . . aerospace booms



as against the 1965 average of 4.8 percent. (This rate was one of the lowest regional rates in the entire country.)

High flier

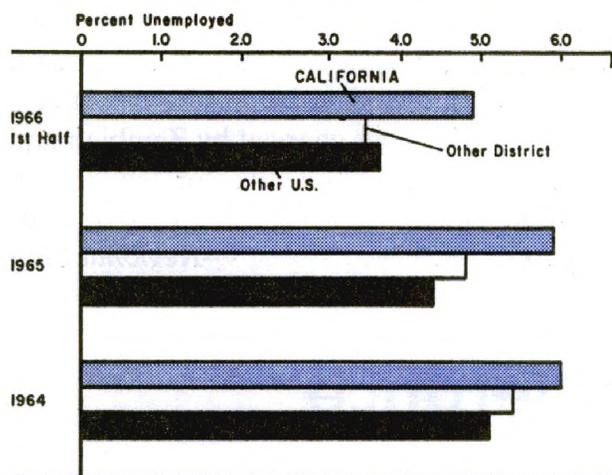
Aerospace-manufacturing firms boosted employment by 4 percent during the spring months, and thereby reached a new peak of 646,000 in June. The commercial-aircraft boom rather than defense demand provided the basis for this sharp year-long upsurge in aerospace employment. However, shortages of engines and aircraft parts are now delaying deliveries of some commercial aircraft, and these production difficulties could dampen the earnings picture for the major aircraft producers.

The war in Vietnam exerted a smaller impact on Western manufacturing than it did elsewhere, although it continued to stimulate a sharp expansion in shipping and related activities. District defense manufacturers chalked up a 10-percent year-to-year gain in prime contract awards, to \$1.8 billion, in the first quarter, but this gain was quite modest in terms of the total national increase. Consequently, the Western share of defense contracts dropped from 31 to 26 percent of the total between early 1965 and early 1966.

Even keel?

Regional housing activity continued to slump during the spring quarter, but a rise in activity in other sectors kept total construction on an even keel. Residential construction awards dropped 17 percent, in dollar terms, as declines occurred in both single-family and multi-family awards. (The pattern of decline was somewhat spotty, however, since housing activity boomed in the Northwest states during this period.) Non-residential construction awards, meanwhile, increased by 27 percent, mostly on the basis of several large contracts for dam construction.

Jobless rate drops sharply as business expansion continues



The West's three-year-long housing slump, initiated by the over-built condition of many communities but aggravated recently by the drying-up of mortgage money, shows up clearly in regional statistics on the number of housing units authorized by new building permits. Between the 1963 peak and early 1966, the West sustained a one-third decline in single-family permits and an even sharper two-thirds decline in multi-family permits. Yet, elsewhere in the country, single-family permits increased slightly and multi-family permits rose significantly higher over the same three-year period, and no drop-off in activity occurred until the spring of this year.

Basic producers

In the District's farm sector, receipts lagged behind the year-ago level during the second quarter, after rising substantially during the earlier months of the year. During the spring months, crop receipts declined as vegetable prices dropped to more normal levels, while livestock receipts continued high on the basis of a strong price situation. But elsewhere in the nation, total farm receipts continued at a very high level.

The Western lumber industry witnessed a strong reversal of the first-quarter price run-up during the spring and early summer months. Defense and construction needs, plus labor

uncertainties, had contributed to the earlier increases—a 25-percent year-to-year price rise for lumber and a 37-percent rise for plywood. But almost half of the lumber-price increase, and practically all of the plywood-price rise, disappeared in the wake of the nation's housing decline and the industry's labor contract settlement.

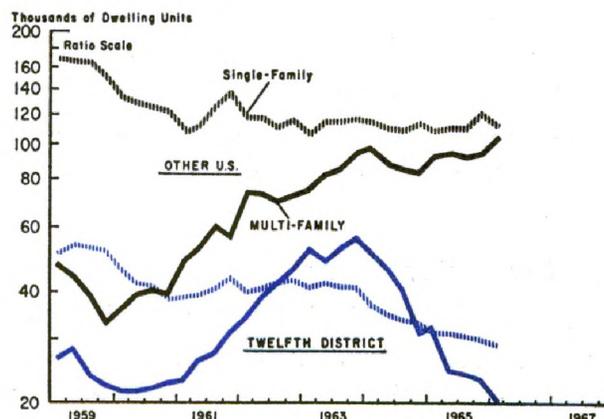
Crude petroleum output in the District ran 10 percent above year-ago levels during the spring months. Jet fuel requirements for military and civilian planes accounted for a significant share of the increased demand. Moreover, military requirements for residual fuel oil contributed substantially to market strength.

Pouring more metal

Western steel producers boosted output during the second quarter to meet the growing demand for defense items (such as tanks and aircraft landing mats) and for structural steel for commercial and industrial building. During the January-June period as a whole, Western steel production ran only 4 percent below the high early-1965 pace, which was dominated by heavy inventory hedge-buying, and steel consumption thus ran at least level with the year-ago consumption figure.

Aluminum producers in the Pacific Northwest raised their primary production to record levels this spring in response to growing mili-

Western housing slump persists, even after three years of decline



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tary and civilian demand. Future capacity requirements also gained attention, as the start-up of a 76,000-ton potline at Bellingham launched a new primary producer into the industry.

Western copper producers expanded output during the quarter to help meet the severe copper shortage, and the Administration also worked to this end by releasing 100,000 tons

of stockpile metal. Nonetheless, pressures on the domestic producers' price, currently 36 cents a pound, intensified when Chile raised its export price from 62 to 70 cents a pound, in a move designed to bring Chilean quotes into line with prices charged by Zambian and Congo producers. But the foreign supply situation—and prices—began to ease by mid-August. —*Regional Staff*

Regional Exuberance

THE Western financial scene was eventful, to put it mildly, in the spring and early summer months. Amid a national environment of increasing monetary pressures, rising interest rates, and intensified competition for deposits, Twelfth District weekly reporting banks expanded their security holdings by more than \$400 million—and their loans by close to \$1 billion—during the April-June quarter. Moreover, they increased their total deposits by \$835 million during this period (daily average basis), even in the face of April's record monthly decline in private time deposits. But more surprisingly, District banks had a \$6-million net *free* reserve position, while in contrast, banks elsewhere recorded net *borrowed* reserves of \$330 million (daily average basis).

Under the impact of extremely heavy business credit demands, regional lending activity accelerated; District bank loans increased almost 4 percent in the second quarter on the heels of a 1-percent first-quarter gain. And in practically all categories, the lending pace in both quarters was above the strong 1965 pace.

On the factory floor

In the first half of 1966, durable-goods manufacturers borrowed at twice their year-ago pace, and thereby accounted for the lar-

gest part of the overall gain in business loans. In particular, borrowing was very substantial in the transportation equipment, fabricated metals, and machinery categories, because of heavy defense demand in those industries.

Nondurable-goods manufacturers also increased their borrowings; food processors recorded an unseasonably small second-quarter loan decline, and petroleum processors meanwhile expanded their borrowings heavily. (The oil industry has now increased its outstanding bank debt by two-thirds over the past year.) The miscellaneous category, which includes mostly service firms, also recorded a sharp expansion during the quarter.

In the face of these strong credit demands as well as the rising cost of bank funds, business-loan rates moved to a postwar peak during the quarter. In early June, District metropolitan banks charged an average rate on short-term loans of 5.89 percent—84 basis points above the year-ago level and 27 basis points above the earlier (June 1960) peak. The June survey reflected the two earlier (December and March) increases in the rate charged to prime business borrowers. However, that survey preceded the late-June and mid-August hikes in the prime rate, so if another survey were made today it would undoubtedly show an even higher level of rates.