MONTHLY REVIEW

BUSINESS CONDITIONS IN THE TWELFTH FEDERAL RESERVE DISTRICT

Federal Reserve Bank of San Francisco *October 1, 1937*

Review of the Month

Volume of industrial production in the Twelfth Federal Reserve District was lower in August than in July, owing to decreased production of lumber. The value of new private building also declined. While these indications of a decline in business activity were reported, consumer buying expanded moderately and cash income received by farmers also increased, continuing to exceed returns of a year ago.

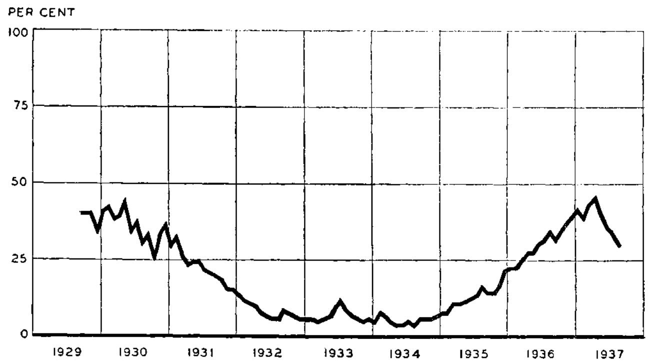
Industry and Trade

After allowance for seasonal influences, industrial output in August was somewhat lower than in July, principally because of curtailed operations in the lumber industry. Lumber production customarily expands substantially at this time of year, and as a result of the contra-seasonal decline this bank's adjusted index fell from 102 percent of the 1923-1925 average in July to 87 percent in August. Some of the curtailment in lumber output reflects an adjustment of operating schedules at mills to a recent decline in orders received and on hand. In addition, labor disputes affected mill activity in several localities in the Pacific Northwest and interruption of commerce with the Orient was also a restricting influence. Notwithstanding a nearly continuous decline in new orders since last April, mill activity has been maintained at a comparatively high rate during recent months with the result that by the end of August unfilled orders had been reduced to the lowest level since November 1935. Mill inventories of lumber have increased more than seasonally since June and prices have tended slightly lower.

In a number of other important manufacturing industries production was maintained through August at a high level, and, except in the cement, flour milling, tire and tube, and sugar refining industries, volume of output generally was higher than in August 1936. California canners were active processing pears and cling peaches. The 1937 peach pack is estimated by trade sources to approximate 12,000,000 cases, the largest since 1930. Near-final reports from salmon canners to the Bureau of Fisheries indicate that this year's pack of Alaska salmon, while not so large as in 1934 and 1936, will be about 14 percent larger than the 1927-1936 average.

Industrial employment in Pacific Coast states, excluding the fruit and vegetable canning industry, declined slightly from mid-July to mid-August, after allowance for seasonal influences. This decline was largely the result of a reduction of three percent in the number of workers at sawmills and logging camps. Pay rolls expanded somewhat, but the increase was less than seasonal. Both employment and pay rolls in the fruit and vegetable canning industry increased further. Operations in this highly seasonal activity usually reach their peak in August.

Value of permits for residential buildings, adjusted for seasonal variations, receded further in August to the lowest level of this year. The adjusted index for August was 29 percent of the 1923-1925 average, compared with 45 percent last April when residential building activity was higher than at any time since 1929. The value of contract awards for private and public nonresidential building also declined and was lower in August than in any month since early 1936. Awards for heavy engineering construction, which included contracts for Ruby Dam, a Seattle municipal project on the Skagit River, advanced substantially.



RESIDENTIAL BUILDING PERMITS
Monthly index of value of permits issued in 18 district cities, adjusted for seasonal variation. (1923-1925 average=100).

Available measures indicate an expansion of consumer purchases during August. Value of department store sales increased more than seasonally, and the adjusted index of furniture store sales was higher in August than in any month since late 1929. The number of new motor vehicles sold in the district was about the same as in July and was seven percent higher than in August 1936.

Railroad business, as measured by the number of freight cars loaded, increased less than seasonally in August. The decline in the adjusted index resulted mainly from sharply reduced shipments of forest products.

Agriculture

Further increases in crop production estimates reported as of September 1 indicate that total harvest of Twelfth District crops will be considerably larger in 1937 than in any recent year. Farmers expect record crops of beans, cotton, potatoes, rice, apricots, pears, almonds, and walnuts, and it is probable that wheat, hops, sugar beets, and grapes will be harvested in near-record volume. The California-Arizona citrus crop, reduced considerably by low temperatures last winter, is the only major crop that will be materially smaller this year than last.

Prices paid farmers for their products in August and September were lower than earlier in the summer but generally higher than a year ago. The United States Department of Agriculture now estimates that 1937 cash farm income in states of this district will be approximately $1,100,000,000. This preliminary estimate is 15 percent larger than 1936 income and higher than in any year since 1929 when the total was about $1,208,000,000.

This year's wheat crop of 120,600,000 bushels is the largest since 1928. Prices being paid wheat growers currently are lower than at the beginning of this season but are slightly higher than a year ago. The record bean crop of 6,294,000 bags is bringing prices about 20 percent lower than a year ago.

Total output of deciduous fruits and nuts is estimated to be of record volume this year. Production of apples was forecast at 49,823,000 bushels on September 1, about 11 percent larger than last year's crop but 9 percent smaller than average annual output during the five years 1928-1932. Although the apple crop is unusually free from worm damage, sizes are smaller than is customary at this date owing to the late season. Harvesting of prunes progressed during August and September with field reports indicating fruit to be of good size. Outturn is expected to be 238,600 tons, compared with 184,300 tons harvested in 1936 and an average production of 226,140 tons from 1928 through 1932.

The condition of livestock ranges declined seasonally during August but most ranges have a good supply of feed and stock water. Winter range feed is dependent, as usual, upon fall and early winter rains. Cattle and sheep generally were in good condition on September 1, according to reports from growers.

Credit

An increase in loans of member banks in leading cities during the five weeks ending September 22 reflected mainly a continued growth in demand for credit from commercial, industrial, and agricultural borrowers. The increase during these weeks appeared chiefly at banks in San Francisco and Seattle, but commercial loans at banks in other leading cities have advanced moderately since early July. Scattered reports of loans at banks in country districts indicate that they also are experiencing considerable expansion in demand for credit.

Loans of Reporting Member Banks
(In millions of dollars)

	1937			1936
	Sept. 22	Aug. 18	June 30	Sept. 23
Total loans	1,046	1,031	1,015	957
Commercial, industrial, and agricultural loans	377	365	345	*
Open market paper	35	35	34	*
Loans to brokers and dealers in securities	23	22	22	15
Other loans for purchasing or carrying securities	57	57	58	*
Real estate loans	368	368	375	364
Loans to banks	2	2	2	1
Other loans	184	182	179	*

*Comparable data not available.

Increases in loans for business purposes are usual at this time of year. In agricultural sections, this is the most important harvesting and marketing season, and borrowings customarily expand markedly to be liquidated in the autumn as payments for crops are received. City banks also are called upon to meet seasonal needs of commercial enterprises. Flour milling concerns and grain dealers seek funds with which to finance wheat purchases. Loans are also obtained in order to carry canned goods, particularly salmon and fruit and vegetables. Many retail merchandising establishments tend to increase inventories in the late summer and fall and seek bank accommodation to finance their larger purchases.

Loans other than for commercial, industrial, and agricultural purposes were practically unchanged during the five weeks under review. Total investments declined considerably less than in other recent weeks, moderate further reductions in holdings of United States Government obligations being largely offset by increased holdings of other securities.

The first change in the discount rate of the Federal Reserve Bank of San Francisco since February, 1934 became effective on September 3. At that time the rate was reduced from 2 percent to 1½ percent. A similar reduction of ½ percent was made at all but one of the other Federal Reserve banks in late August or early September. The discount rate now stands at 1½ percent at all Federal Reserve banks except New York, where it is 1 percent.

During the last four months of each year, Twelfth District banks, like banks in other parts of the country, are called upon to meet a considerable withdrawal of coin and currency for circulation. This increase of money in circulation arises from seasonal expansion in retail trade and other activities which involve relatively large payments in currency. Demand for currency in the Twelfth District increased $13,888,000 from September 1 to December 26, last year and $19,138,000 during the comparable period in 1935. These seasonal requirements for additional currency result in drains upon member bank reserve balances, and they occur in large part at the same time that banks are being called upon to make additional business loans. Since increased loans tend to increase deposits, reserve requirements are therefore likely to increase at the same time. Both of these factors have a tendency to place limitations upon the making of additional loans or the increase of investment holdings, particularly among banks without considerable excess reserves.

In the past few years member banks have met fall currency and loan demands with extreme ease because of the presence of large amounts of idle reserves. During the past year, however, idle reserves of district member banks have been reduced considerably, although they still total about 16 percent in excess of legal requirements. In addition, balances with correspondents in excess of operating needs have been reduced during the past year.

Production and Employment—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment			Without Seasonal Adjustment		
	1937		1936	1937		1936
Industrial Production	Aug.	July	Aug.	Aug.	July	Aug.
Manufactures (physical volume)						
Lumber†	87	102	79	107	107	93
Refined Oils*	—	—	—	166	163	166
Cement*	—	106	106	—	116	118
Meat*	117	116	111	—	—	—
Wheat Flour*	119	106	134	119	94	134
Minerals (physical volume)						
Petroleum*	—	—	—	102	101	88
Lead (U. S.)*‡	—	82	60	—	79	58
Construction (value)						
Urban residential building permits in 18 cities*	29	34	34	29	31	34
Public Works Contracts*	—	—	—	212	137	199
Miscellaneous						
Electric Power Production*	208	203	187	229	227	205

*Daily average. ‡Prepared by Board of Governors of the Federal Reserve System. †Revised series.
Note: Series on employment and pay rolls, usually published in this table, are in process of revision.

Although these reductions have by no means eliminated excess reserves for district banks as a whole, their distribution is not so widespread nor uniform as in other recent years. Consequently, some of the banks experiencing increased demands because of seasonal expansion in currency and loans may need to obtain funds in order to maintain reserves at the required level.

District banks seeking to increase or maintain their reserves may pursue several alternatives. They may obtain loans from correspondents or from banks in the large money centers of the country, particularly New York; they may dispose of earning assets, especially those upon which they receive a low rate of return, either within the district or in other sections of the country; they may borrow from the Federal Reserve Bank of San Francisco.

The course followed by a bank in obtaining funds will be influenced to some extent by the relative costs of the several alternatives. Recent action in reducing the discount rate brings the cost of borrowing at the Federal Reserve Bank of San Francisco closer to the rate at which funds may be borrowed in the principal money markets of the country. It also brings the discount rate nearer to the return the banks are receiving on their lower yield investments. As a result, local bankers are encouraged to extend loans at continued low rates of interest and to refrain from drawing upon the resources of banks in other areas either through borrowing or through sale of earning assets.

Financing of Security Transactions in the Twelfth District

Security transactions in the Twelfth Federal Reserve District involve the purchase and sale of securities in local and eastern markets. Most of the transactions are handled by brokers and dealers with offices in this district. Some of these offices are local branches of New York firms; some are branches of national organizations which have their head offices in the district; and some are firms which are entirely local in their scope.

Distribution and Trade—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment			Without Seasonal Adjustment		
	1937		1936	1937		1936
Retail Trade	Aug.	July	Aug.	Aug.	July	Aug.
Department Store Sales (value)*						
Twelfth District	98	97	92	94	79	88
California	105	102	99	103	84	97
Los Angeles	102	95	92	101	82	91
Bay Region	109	108	107	107	88	105
San Francisco	108	105	106	104	86	102
Oakland	114	117	111	121	92	118
Pacific Northwest	75	78	72	68	61	65
Seattle	90	88	80	82	70	73
Spokane	62	63	61	58	49	58
Salt Lake City	81	77	75	64	56	60
Department Store Stocks (value)†	72	72	64	70	68	62
Furniture Store Sales (value)*‡	97	94	92	100	87	95
Automobile Sales (number)*						
Total	—	—	—	140	144	131
Passenger	—	—	—	130	133	119
Commercial	—	—	—	252	255	256
Carloadings (number)*						
Total	90	96	85	105	97	100
Merchandise and Misc.	97	99	94	114	105	110
Other	82	94	75	94	87	86
Intercoastal Traffic (volume)						
Total	73	64	77	76	70	81
Eastbound	57	55	62	60	60	66
Westbound	127	101	128	130	103	130

*Daily average. †At end of month. ‡1929 average=100.

Since October 1935, monthly figures have been collected by the Federal Reserve Bank of San Francisco concerning funds loaned by brokers in the Twelfth District to their customers. Figures are received from New York Stock Exchange, San Francisco Stock Exchange, Los Angeles Stock Exchange, and San Francisco Curb Exchange members whose head offices are located in this district. While a considerable number of brokers operating in the district are not included in this group, reporting brokers carry a large proportion of the margin accounts outstanding. On the basis of these reports, the following composite balance sheet has been prepared as of October 31, 1935 and August 31, 1937. Some offsetting items such as inter-borrowing between local brokers have been eliminated.

COMPOSITE BALANCE SHEET
TWELFTH DISTRICT REPORTING BROKERS

Assets	Oct. 31, 1935	Aug. 31, 1937
Cash	$ 6,345,000	$ 8,013,000
Securities owned	8,755,000	9,139,000
Loans to customers	36,387,000	67,229,000
Loans to partners	2,094,000	1,835,000
Other assets (net)	5,419,000	5,092,000
Total	$59,000,000	$91,308,000
Liabilities		
Loans from New York banks	$ 8,112,000	$25,763,000
Loans from local banks	7,146,000	15,631,000
Loans from New York brokers	9,106,000	12,466,000
Loans from others	1,138,000	948,000
Credit balances of customers*	13,827,000	14,172,000
Credit balances of partners	422,000	495,000
Capital accounts	19,249,000	21,833,000
Total	$59,000,000	$91,308,000

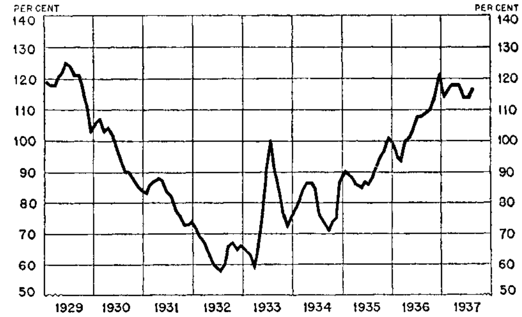
*A large proportion of the credit balances of customers is subject to immediate withdrawal. The remainder primarily represents uncompleted transactions, short sales, and margins on commitments in commodities and unissued securities.

As is shown by this balance sheet, the assets and liabilities of reporting brokers increased by about 55 percent between October 31, 1935 and August 31, 1937. The increase reflected principally an 85 percent increase in loans to customers.

In addition to loans made to customers by reporting brokers, a considerable amount of credit is extended to customers by local branches of New York Stock Exchange members whose head offices are located outside this district. A smaller amount of funds is borrowed by customers from local non-reporting firms, while many brokers and dealers borrow for their own account from banks and other lenders. By means of special reports and estimates, an approximation of the total amount of funds borrowed in the Twelfth District for the purpose of purchasing securities has been obtained. In the following table these funds have been segregated according to the groups which utilize them and the types of lenders which furnish them. The figures do not include private transactions between individuals, which are of minor importance.

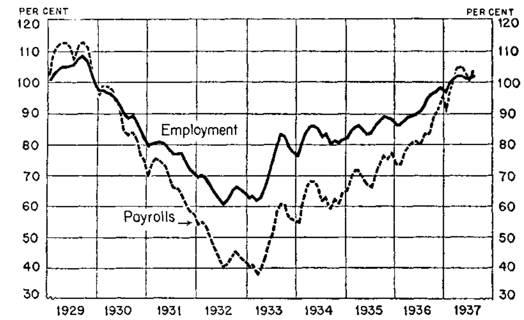
FINANCING OF SECURITY PURCHASES IN TWELFTH DISTRICT

Funds Borrowed:	Aug. 31, 1937
By customers from brokers	$102,000,000
By customers of brokers and dealers from banks	67,000,000
By brokers and dealers from banks and other lenders for own account	11,000,000
Total	$180,000,000
Sources of Funds Borrowed:	
New York banks and brokers	$ 56,000,000
Local banks	95,000,000
Local customers of brokers	28,000,000
Other lenders	1,000,000
Total	$180,000,000



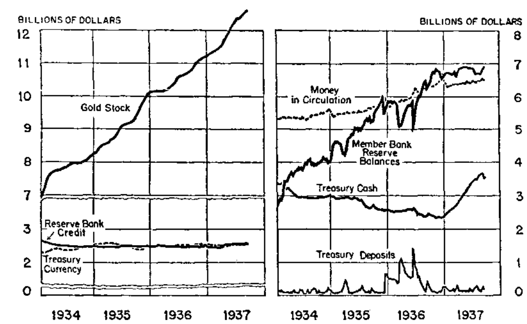
INDUSTRIAL PRODUCTION

Index of physical volume of production, adjusted for seasonal variation, 1923-1925 average=100. By months, January 1929 to August 1937.



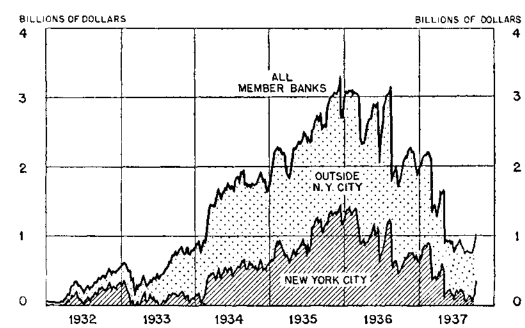
FACTORY EMPLOYMENT AND PAY ROLLS

Indexes of number employed and pay rolls, without adjustment for seasonal variation, 1923-1925 average =100. By months, January 1929 to August 1937. Indexes compiled by the United States Bureau of Labor Statistics.



MEMBER BANK RESERVES AND RELATED ITEMS

Wednesday figures. January 3, 1934 to September 22, 1937.



EXCESS RESERVES OF MEMBER BANKS

Wednesday figures of estimated excess reserves for all member banks and for New York City January 6, 1932, to September 22, 1937.

Summary of National Business Conditions

Prepared by the Board of Governors of the Federal Reserve System

In August, industrial activity advanced from the level of the two preceding months and on a seasonally adjusted basis was close to the volume of last spring. Early reports for September indicate a decline in steel output and a seasonal decrease in the production of automobiles.

Production and Employment

Volume of industrial production, as measured by the Board's seasonally adjusted index, was 117 percent of the 1923-1925 average in August as compared with a level of 114 percent in June and July and 118 percent during the spring. Steel production rose slightly further and was close to the high level prevailing before strikes curtailed output in June. Automobile production was maintained in considerably larger volume than is usual in the month preceding the shift to new model production. Lumber output declined, following a period of increase. In the nondurable goods industries output increased in August, reflecting chiefly increases at cotton and woolen textile mills, following considerable declines in the preceding month. Activity at meat packing establishments increased somewhat from an extremely low level. Shoe production showed less than the usual seasonal rise. At mines, output of coal increased less than seasonally, while crude petroleum production continued to expand.

Value of construction contracts awarded, as reported by the F. W. Dodge Corporation, declined somewhat in August and the first half of September. Awards for private residential buildings showed little change and were in about the same volume as in the corresponding period of 1936, while publicly-financed residential building declined and was in considerably smaller volume than last year.

Factory employment, which had increased in July, showed less than a seasonal rise in August. Factory pay rolls increased by about the usual seasonal amount. The number employed at steel mills increased somewhat further, while at automobile factories, railroad repair shops, and sawmills employment declined. In the textile industries, employment in the production of fabrics decreased somewhat, while employment in the production of wearing apparel increased. Changes in employment in most other manufacturing industries were small.

Agriculture

Department of Agriculture crop estimates based on September 1 conditions were about the same as the estimates a month earlier, except for an increase in cotton and a decrease in corn. Output of leading crops is substantially larger than last season. Supplies of livestock and meats are expected by the Department of Agriculture to continue smaller than last year.

Distribution

Mail order sales and sales at department stores showed somewhat less than the usual seasonal increase from July to August. Freight carloadings continued at the level of the previous month.

Commodity Prices

Cotton prices declined considerably further from the middle of August to the third week of September and there were smaller decreases in cotton goods, silk, hides, steel scrap, copper scrap, and lumber. Prices of livestock and livestock products, after some decline in the latter part of August and the first week of September, advanced sharply in the middle of September.

Bank Credit

Excess reserves of member banks increased in the five-week period ending September 22 from $800,000,000 to $1,000,000,000 as the result of a release of gold by the Treasury from its inactive account. The bulk of the increase in excess reserves went to New York City banks and on September 22 these banks had excess reserves of $350,000,000, Chicago banks had $50,000,000, and banks elsewhere $600,000,000.

Commercial loans at reporting member banks in 101 leading cities, reflecting in part seasonal demands, continued to increase substantially during the four weeks ending September 15, both in New York City and outside. Holdings of United States Government obligations and of other securities showed a further decrease, with the result that total loans and investments declined somewhat.

Money Rates

Rates on nine-month Treasury bills declined from 0.71 percent early in September to 0.44 percent later in the month, and average yields on long-term Treasury notes declined from about 1⅝ percent to below 1½ percent.