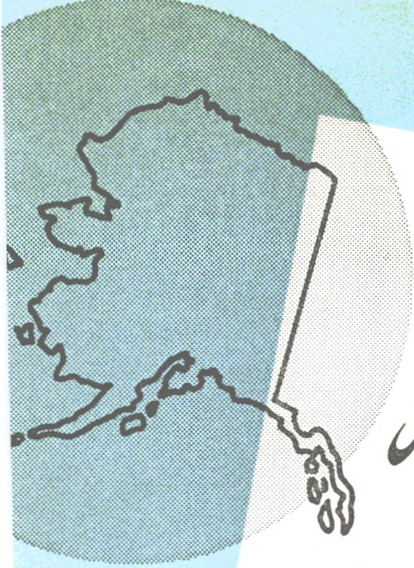
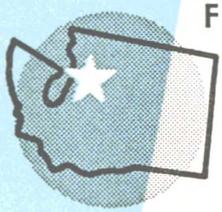
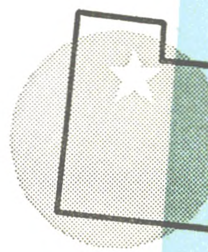


Monthly Review

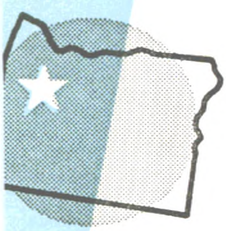
FEDERAL RESERVE BANK OF SAN FRANCISCO
TWELFTH FEDERAL RESERVE DISTRICT

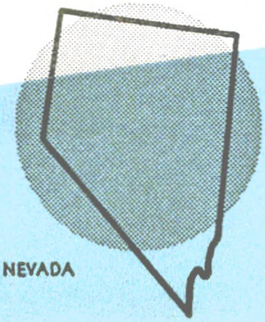


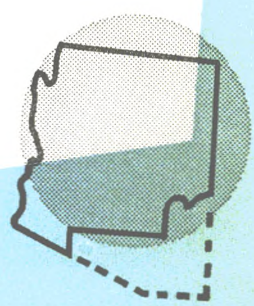


July 1962

In This Issue







Review of Business Conditions

THE 15th of the month is always an interesting day for economists and observers of the business scene for it is on or about this day that many of the statistics concerning the state of the economy in the past month become available. The economist, unlike the soothsayer of old, must content himself with information of weeks past rather than more occult indicators such as the entrails of the sacred fowl or the phases of the moon or the stations of the stars. It is more difficult yet necessary to look for causal relationships rather than supernatural manifestations, and the statistics for the month of June are of particular interest in view of the recent behavior of the stock market.

The Council of Economic Advisers reported that gross national product for the second quarter was $552 billion at a seasonally adjusted annual rate, up $7 billion from the first quarter rate and a slightly larger dollar increase than was recorded in the first quarter. The second quarter figure was about $10 billion below the Administration forecast made at the beginning of the year. Purchases of consumer durable goods rose after a decline in the first quarter of the year, and other consumer spending continued to rise. Business expenditures for plant and equipment continued to gain in the second quarter as did the purchase of goods and services by all levels of government. Impressive increases occurred in spending on new construction, particularly residential. The expansion in total spending was retarded by a sharp drop in the rate of business inventory accumulation, which at an annual rate of $3.5 billion for the second quarter was little more than half the rate of accumulation in the first quarter.

The index of industrial production was 117.8 percent of the 1957 average in June, up slightly from 117.5 percent in May. There were declines of 8 percent in automobile assemblies and in iron and steel production. The drop in auto output was due in part to a 2½ week strike affecting one of the major producers. The principal gains were in the output of business equipment, construction materials, and most nondurable goods. New factory orders for durable goods in June fell off about 3½ percent from May levels, making the fifth successive monthly decline in this series. The July survey of the National Association of Purchasing Agents indicated that the levels of new orders and production declined for the third month. Manufacturers inventories increased $100 million during June, the smallest monthly gain since August 1961. Manufacturers sales declined 2 percent in June.

Construction put in place in July was estimated to be almost $61.7 billion at a seasonally adjusted annual rate, representing a decline of 1.3 percent from the record June rate. Private construction spending rose slightly in July while public construction fell by 5 percent. Advance indicators in the construction sector do not present a picture that presages an expanding volume of residential construction in coming months. Housing starts in June declined by 11 percent from May levels to a seasonally adjusted annual rate of 1,389,000 units. This is the first decline in this series since February. FHA applications for mortgage insurance on new homes were running at an annual rate of 212,000 in June, down about 9 percent from May. This was the third consecutive monthly decline and brought the rate of applications to the lowest level since July 1957. VA appraisal requests were 14,725 in June (not seasonally adjusted), a decrease of 17 percent from the previous month. Mortgage funds continue to be abundantly available, however, on terms that are somewhat easier.

Nonfarm payrolls increased by 500,000 in June to a record level of 55.7 million workers. However, on a seasonally adjusted basis the gain was only 43,000, the smallest month-to-month increase this year, and the average length of the factory workweek fell off slightly during the month, down to 40.4 hours from 40.6 hours in May. At the same time, the actual number of unemployed rose by 744,000 to 4,463,000 as June graduates and teenagers swelled the labor force. Unemployment as a percentage of the total labor force stood at 5.5 percent in June, up 0.1 percent from May. Preliminary employment figures for July struck a more positive note. There was little change in total employment, but unemployment declined by about 450,000. The seasonally adjusted rate of unemployment dropped to 5.3 percent of the labor force, the lowest rate since May 1960.

Personal income reached a seasonally adjusted annual rate of $440.4 billion in June, up $700 million from May but the smallest increase registered this year. This reflects the slowdown in steel output during the month. Retail sales decreased in June for the second straight month, falling to a level of $19.1 billion, a 2 percent decline from May. The decline was most prominent in the sale of durable goods which were down by about 5 percent from May levels. Although new car sales in June were the highest for this month since 1955, they failed to show expected seasonal gains from May. Data for the first 15 trading days of July showed a daily average selling rate of autos that is slightly below the comparable period in June. However, department store sales rose to 115 percent of the 1957-59 average in July, an increase of 3 percent from June and equal to the May level. Department stores sales often move parallel to total retail sales and this may imply that retail sales will show a rise in July.

The figures available on the state of the economy in mid-July are not altogether conclusive: they tell not one but many stories. On balance, the picture was one of modest expansion but at a slower rate than in earlier months. This was evident even in the stock market during the latter part of June and the first days of July, although stock prices turned down again in the second week of the month. The June declines in residential construction and in retail sales may be explained in part by the fact that earlier months showed very substantial gains—May for residential construction and April for retail sales—that might not be expected to be matched in each succeeding month. Personal income has continued to rise and the liquid assets held by the public have shown steady growth, giving consumers the ability to sustain a high level of final demand. Business firms have shown no indication of increasing their expenditures beyond the estimates given earlier in the year. All of the signs are not entirely in the direction of expansion. A slowing in the rate of increase was evident in many sectors together with declines in other areas. The vagaries of the stock market in recent weeks and months may be either a cause or a symptom of the slowing in the rate of growth in the economy; the slow rate of growth in business activity may have had a depressing effect upon stock prices and the decline in stock prices may have had some influence on the expectations of individuals and business firms, though there is no clear-cut evidence of this to date. Such a combination of cause and effect or "feedback" is not uncommon in a complex and highly organized economy. Additional information on the July figures should help clarify the diagnosis.

District employment dipped in June

The number of nonfarm wage and salary workers employed in the District (excluding Alaska and Hawaii) declined 0.4 percent from May to June, principally as a result of labor disputes affecting construction workers. Slight gains occurred in trade, finance, services and government employment while manufacturing, mining, and transportation jobs decreased.

Contract construction employment dropped 6.4 percent in June after declining 3.7 percent from April to May. The protracted labor-managament dispute in northern California accounted for most of the shrinkage in construction employment, although this was reinforced by labor disputes during June involving ironworkers in western Washington and Oregon and carpenters in Nevada.

The construction strike and lockout apparently had its greatest impact on initial claims for unemployment insurance in May, followed by a rise in the number of insured unemployed workers in June. Initial claims for unemployment insurance benefits declined 2 percent in June from May, after seasonal adjustment. The average weekly volume of initial claims in May—56,800—was the highest since July 1961. Average weekly insured unemployment for the whole District rose from 295,900 in May to 326,000 in June, an increase of 10 percent on a seasonally adjusted basis. This represented 5.7 percent of average covered employment in June, up from 5.2 percent the month before, and paralleled the increase in the rate of total unemployment in the Pacific Coast States.

In June, District manufacturing production workers averaged 40.2 hours per week; the June workweek after seasonal adjustment was 40 hours, the same as in May but 0.3 hours longer than in June 1961. Hourly earnings rose by 1 cent to $2.77. Although this was 8 cents above a year ago, it was only equal to the average which prevailed in the first 6 months of this year. Average weekly earnings were $111.35, $4.02 higher than last June.

In June, another major labor market area in the District, San Bernardino-Riverside-Ontario, was shifted from the "substantial unemployment" category to the classification of "moderate unemployment." Contributing factors in the reclassification of the area were the advance during the last 12 months in primary metals and electrical machinery manufacturing and seasonal hirings in agriculture and construction. A sharp reduction in joblessness was responsible for the removal in June of Oxnard, California from the list of smaller areas of substantial unemployment. These improvements in the labor market conditions in the District were further reflected by the small number of major areas classified as having "substantial unemployment" now remaining in the District, four in June 1962 compared with ten such areas in June 1961.

Pacific Coast unemployment rose in June

Total civilian employment on the Pacific Coast declined by 0.4 percent from May to June, on a seasonally adjusted basis. Agricultural employment fell by 1.5 percent, primarily because the maturing of crops was delayed by cool weather in the spring months. Total nonagricultural employment dipped slightly in June; most of the decline was attributable to the labor-management disputes in the construction industry in all three states.

Unemployment on the Pacific Coast increased by 32,000 persons in June, or 6.7 percent, raising the seasonally adjusted rate of unemployment from 5.7 percent of the labor force in May to 6.1 percent in June. June was the first month since December 1961 that the rate of unemployment had reached or surpassed 6 percent. This rise was strongly influenced by the delay in such seasonal work as agriculture and food processing resulting from late crops and by unemployment induced by strikes in construction. After seasonal adjustment, the civilian labor force on the Pacific Coast was unchanged from May to June. It had grown by 0.8 percent from the same month last year, but the rate of growth from a year ago was slightly off the pace set in the first five months of 1962.

Manufacturing employment on Pacific Coast unchanged; defense industries expanded

Total manufacturing employment on the Pacific Coast remained virtually unchanged from May to June. A moderate rise in durable goods manufacturing, particularly in electrical machinery and transportation equipment, offset a loss in nondurable goods, primarily in food and kindred products.

Employment in the defense-related industries, which are concentrated in California and Washington, continued to expand in June and was 0.6 percent above May and 10 percent higher than in June 1961. Although aircraft employment in California fell by 400 employees from the May level, the industry in Washington in June added 1,100 workers to the payrolls. These hirings brought total employment in aircraft in the state to 75,000, topping the previous record of January 1959.

In the first six months of 1962, total employment in the defense industries on the Pacific Coast has increased by an average of 43,000 workers, or 8½ percent, over the like period in 1961. Almost half of the gain occurred in electrical equipment, and one-fourth in ordnance employment in California. The comparison with the first six months of 1960 clearly shows the changing complexion of the defense industries, which are moving away from high employment in aircraft and parts toward increasing employment in electronics and missiles. Over the two-year period, employment in aircraft has declined by 3 percent, with all of this loss occurring in California plants. In contrast, employment in electrical equipment has risen by 16 percent, and ordnance employment in California has experienced the greatest relative growth, up 35 percent.

DEFENSE-RELATED EMPLOYMENT, PACIFIC COAST MANUFACTURING

(thousands of employees)

	Average for first 6 months 1962	1961	1960
Electrical equipment	201.1	180.6	173.1
Aircraft and parts	265.6	254.0	274.8
Ordnance (California)	78.5	67.7	58.3
Total	545.2	502.3	506.2

Source: California, Oregon and Washington Departments of Employment.

District construction strong but temporarily depressed by strike

The dollar volume of contract awards in Region 8 (the Twelfth District less Alaska and Hawaii but including Montana, Wyoming, Colorado, and New Mexico) declined in June from the level of May. Although nonresidential contract awards continued to rise moderately, residential contracts fell by 15 percent. This decline reflects the eight week construction strike in northern California which ended on June 27. For the first half of this year, the value of nonresidential contracts was 6.5 percent ahead of the same period in 1961 and residential contracts were 20 percent above. This experience is about the same as in the nation where comparable figures were plus 11 and plus 18 percent, respectively.

On a monthly basis, February contracts were exceptionally low in the District, as in the country, and March showed a very large gain with changes moderately upwards in April and May. California and Washington show consistently higher levels of awards this year as compared with 1961 while other District states are lagging behind their earlier highs. Nonresidential construction is most markedly ahead of a year ago in southern California, Idaho, Oregon, and Washington. Engineering contracts in the Far West declined in June but remained at a relatively high level. For the first half of the year such contracts were about even with last year.

Another guide to District housing activity is provided by tabulations in selected areas of residential building permits. Among the 13 areas regularly reviewed, most showed increases from May to June, and for the first half of the year permits in most areas were well ahead of year-ago figures. The only areas for which this is not true are those characterized as overbuilt last year: San Diego, Stockton, and Sacramento. The impact of the construction strike is evident in San Francisco, where permits fell by 58 percent in June, and in Oakland where they declined by 15 percent. FHA applications for mortgage insurance on new housing have picked up steadily in the first five months of this year but are lagging behind last year's pace. FHA applications on existing housing, on the other hand, exceeded year-ago figures by a considerable margin.

Mortgage funds abundantly available

The pressure of increased savings seeking outlet but requiring the relatively high yield of mortgages continues to be evident in the District as in the nation. Savings accounts at reporting savings and loan asssociations in the District rose sharply from May to June. During the first half of this year the increase was well in excess of $1 billion and was 24 percent ahead of the year-ago performance. During the same period, the increase in real estate loans outstanding at these savings and loan associations was 33 percent greater than last year. Borrowings from the Federal Home Loan Bank of San Francisco by these member associations were about 40 percent greater than the year earlier figure. Reported loan commitments, on the other hand, show some tapering off from the heavy gains of earlier months.

Time deposits at District weekly reporting banks increased in the first half of this year by over $1.2 billion, or more than 9 percent. Of this increase, only $659 million represented the rise in savings deposits; and during the same period these banks increased their real estate loans outstanding by $356 million. This experience contrasts with 1961 when savings deposits rose by $437 million but real estate loans outstanding declined. The sizable increases in June at these banks in savings deposits ($146 million) and real estate loans ($76 million) continued in the first three weeks of July as another $141 million net flowed into savings accounts and real estate loans outstanding rose by another $62 million.

Lumber demand strong in May, slower in June

The demand for Douglas fir picked up in May with the uncertainty of the labor situation in the lumber industry lending strength to a market stimulated by strong construction activity. New orders advanced 6 percent over April and stood about 9 percent higher than the level of May 1961. Production rose 7 percent above April but fell behind the increase in new orders and was 4 percent lower than output for May of last year. A 13 percent increase in shipments in May exceeded production for the month and brought about a 5 percent reduction in inventories. At the end of May unfilled orders were equal to 49 percent of inventories on hand, compared with 43 percent a year earlier. Douglas fir production in June fell about 9 percent below the level of output in May and similarly below the June level a year ago. New orders declined about 2 percent during the month but exceeded June production and the level of new orders received in June a year ago. At month end the ratio of unfilled orders to stocks had risen to 52 percent.

Production and new orders for pine lumber rose 19 and 13 percent, respectively, in May. Although May output was slightly below its level in May 1961, production and new orders in the first five months of this year exceeded their levels in the comparable five months of 1961.

The production of California redwood rose slightly in May, but output lagged about 17 percent behind the level of the comparable month a year ago. New orders fell off about 4 percent from April although they were up 8 percent from a year ago. The demand for redwood was restricted in May and June by construction labor problems in California and by the mild interest shown by Eastern buyers of industrial and finished items. Production and new orders for redwood declined 5 and 1 percent, respectively, in June. Rising shipments and declining production resulted in a 4 percent reduction of stocks on hand.

Crow's average lumber price per thousand board feet registered an increase of 91 cents from April 26 to June 21 primarily as the result of higher prices for green and dry fir which increased $1.24 and $1.32 per thousand board feet, respectively, during this period. The average price for various types of pine rose by $0.56 during this same period.

Western steel production affected by construction strike in June

Western steel production was adversely affected in June by the strike in the construction industry. Although the effect upon steel output of reduced demand from the construction industry was moderated by a seasonal rise in demand from the canning industry, production declined 14.7 percent between the week ended June 2 and the week ended June 30. In contrast, national steel production fell off by 5.3 percent during this period to a weekly output level of 1,563,000 tons, the lowest level of production since the week ended February 4, 1961.

Western and national steel production registered further overall declines from the week ended June 30 to the week ended July 21 as major producers closed for the July 4 holiday and the industry entered the traditional slowdown in activity associated with vacations. The 17.5 percent reduction in the national index during the July 4 holiday week was the sharpest weekly percentage decline since industry output fell 20.3 percent during the July 4 holiday week in 1960. Weakness in new orders caused firms in the East and Midwest to close not only for the holiday but for the entire week. The Western index registered a 10 percent decline for the same week. Spurred by a modest improvement in new orders, national production rose in the next two weeks but did not fully recover its preholiday level. Western output also rebounded in the week ended July 14 but registered a 7.1 percent decline in the week ended July 21 in response to summer vacation slowdowns.

May copper production sets record; June demand softens

Production of copper in the United States set a new record in May, rising 10.6 percent above the previous high recorded in April. May shipments to domestic consumers increased by nearly 10 percent, and producers' stocks rose after four successive monthly declines. The demand for copper slackened in June from the level attained in May and further cutbacks extended into July because of vacation shutdowns at consumer and producer plants.

Although a published price of 31 cents a pound for refined copper has been maintained for over a year, world overproduction has been exerting a downward pressure. Metal trade dealers have been pricing refined copper below the producer quotation at about 30⅛ to 30¼ cents a pound for August shipment, and fourth-quarter shipment quotations have been ranging from about 29¾ to 30 cents a pound depending on the month of delivery. The price of copper for immediate delivery on the London Metal Exchange has remained at 29¼ cents a pound for several months but only because of the supporting operations of important African mining concerns.

In view of the fact that world production of copper has reached record levels and is running ahead of world demand, voluntary reductions in production have been announced by three major United States producers and by several African copper producers. It is estimated that these cuts will lower free-world copper output by 8,800 tons a month or a little less than 3 percent of average monthly output in the first five months of 1962.

West Cost petroleum industry quiet in June

West Coast refinery runs declined slightly in late June, arresting a several week rise which had pushed operations above the year-ago level for the first time since last winter. Partly because of the easing, West Coast operations for the month were only slightly higher than in June 1961. This was in marked contrast to the situation nationally, where in the four weeks ended July 6 refinery runs reached their highest level in history. This high level of output, in combination with a recent easing in demand, has contributed to a contraseasonal rise in gasoline stocks. Excluding the West Coast, these stocks are now above year-ago levels for the first time since early last January. Despite this, retail prices nationally appear to have firmed slightly in recent weeks, in contrast to earlier expectations. In the West, areas for which retail price data are available indicate no significant changes in recent weeks.

Farm market receipts at record high level in District

Returns from marketings have displayed unusual strength during the first five months of 1962 with cumulative receipts flowing to District farmers in record volume. District farmers received $367 million from the sale of farm products during the month of May. This was a record level of returns for this particular month and stemmed from increased returns from the sale of livestock and livestock products which were 7 percent higher than a year earlier. Crop prices in mid-May were also higher than a year earlier but the effect on returns was more than offset by reduced marketings. Prices received for both livestock and crops eased from mid-May to mid-June.

Receipts of farmers from the sale of their products is not a full indication of the cash income farmers receive. Government payments are also a source of cash income. Because of the extension of the emergency programs to wheat and barley in 1962, Government payments to District farmers will be considerably larger than the $80 million received in 1961.

Department store sales rose in June and July

During May, sales of Group I retail stores[1] in the Twelfth District were at their highest level of the year, up 5 percent from April and 17 percent from 1961. With the exception of apparel stores, all types of retail outlets showed gains over the April level, with the automotive group having the largest increases. During June, department store sales rose slightly from the May level after seasonal adjustment. Seattle, Tacoma, and San Diego continued to show the largest gains. During the first two weeks of July, sales ran about 8 percent above the year-ago levels. For the nation as a whole, however, department store sales fell by somewhat less than 1 percent from the May rate while the July experience has been roughly comparable to that in this District.

Auto sales picked up in June after poor showing in May

There were 52,375 new cars registered in California during May, down 13 percent

[1] Stores of firms operating 1-10 stores at the time of the 1958 Census of Business.

from the April level in spite of the fact that there were two more trading days. On a daily average basis, the May experience was the poorest for any month since January of this year. However, registrations were still running 10 percent above the year-ago month. Following the usual seasonal pattern, registrations during June picked up and for the first 26 days were at a daily rate of 2,209 compared with 1,795 for the same period of May. National experience differed somewhat from that in California in that sales fell below May during June, although they were at the highest June level since 1955. In the first third of July new car sales nationally were down from the same period of June, which follows the usual pattern.

Consumer credit rose in May

Consumer credit outstanding at District commercial banks continued to reflect through May the influence of automobile financing, although all of the other types of consumer loans also rose. Between the end of April and May, consumer automobile paper held by banks rose $30.1 million with most of the increase occurring in purchased paper. Indications are that through May there has also been some lengthening in the average maturity schedule for these loans. Such lengthening, however, is not unusual as the model year draws to a close. Repair and modernization loans showed a $7 million increase, while personal and consumer goods paper, other than automobile, rose by moderate amounts.

Country banks had larger gains in first half of 1962

Country member banks in the Twelfth District outpaced the Reserve City banks in the first six months of 1962 in the rate of increase in total bank credit outstanding. This was due to a rise of more than 10 percent in loans, about twice the rate for Reserve City banks. The percentage reduction in total security holdings during this period, however, was larger than for the Reserve City banks. Both bank groups reduced their portfolios of United States Government securities but increased their holdings of other securities—country banks by less than 3 percent and Reserve City banks by 17 percent. Country banks had a smaller rate of decline in demand deposits adjusted during the first half of the year than Reserve City banks, but both groups registered an increase in time deposits of slightly over 9 percent. Increased costs resulting from the larger volume of time deposits and the higher rate of interest paid on such deposits beginning in January 1962 have contributed to a decline for many District banks in their net earnings for the first half of 1962 compared with the first half of 1961. Some District banks, however, have been able to increase their gross earnings enough to offset these rising costs. On the basis of available published reports, the first-half earnings picture in the District is mixed, with many of the larger branch banks in the lower net earnings group.

Loans and deposits expanded in June and early July

Data for weekly reporting member banks in the District provide more recent information on banking developments. In the six-week period from May 30 to July 11, total bank credit outstanding continued to expand with most of the gain occurring in loans rather than in investment in securities. Banks continued to seek real estate loans and, as shown in the accompanying table, this category again accounted for the largest increase of any of the loan categories. The substantial rise in commercial and industrial loans during this period reflected, in part, borrowing by business to meet June 15 tax payments. The increase in mid-June in business loans was the largest weekly gain so far this year.

Tax borrowing this year appeared to be somewhat in excess of that in 1961 but less than in 1960.

On the basis of weekly reporting bank figures, the rate of increase in consumer loans (the main component of the "other loan" category) appears to have slowed somewhat in June and early July compared with the first five months of 1962 when consumer instalment credit outstanding at commercial banks in the Twelfth District rose 4 percent. During that period an increase of over 6 percent in automobile loans more than offset a decline in loans to finance other consumer goods paper. Personal loans during this period rose by almost the same percentage. The rate of increase in total consumer instalment credit at District banks in the first 5 months of the year exceeded that of all banks in the nation, and consequently the already high proportion of such credit held by District banks rose to approximately 17 percent of the national total. Table 1 shows the dollar amounts outstanding by type of consumer instalment loan for the nation and for each of the Federal Reserve Districts. Because of the important position of the Twelfth District in this field of bank financing, the dollar changes in the "other loan" category for weekly reporting banks in the District have, in recent months, often accounted for one-half to one-third of the total dollar change in the national series.

In June and the first two weeks of July there was practically no net change in total United States Government security holdings of District weekly reporting member banks. Some increase in holdings in the 1- to 5-year maturity range was due largely to the shift of the 2½ percent "tap" bonds of 1967-72 into this maturity category in mid-June. While net additions were made to other security holdings during this period, the rate of increase was lower than the high rate of March and April.

TABLE 1
CONSUMER INSTALMENT CREDIT AT COMMERCIAL BANKS
(millions of dollars)

Federal Reserve District:	Amounts outstanding May 31, 1962
Boston	910
New York	2,839
Philadelphia	1,160
Cleveland	1,189
Richmond	1,332
Atlanta	1,361
Chicago	2,543
St. Louis	789
Minneapolis	518
Kansas City	830
Dallas	928
San Francisco	2,917
Total	17,316

Contrasting with a decline nationally, demand deposits adjusted at District weekly reporting banks rose more than 2 percent during this period. A sizable reduction in time deposits of states and political subdivisions slowed down the rate of gain in total time deposits at District banks. Savings deposits, on the other hand, registered a large increase as interest was credited at mid-year. Savings deposits increased $41 million in the second week of July indicating that whatever withdrawals of interest may have occurred after June 30 were more than offset by new deposits.

In June, District banks were net sellers of Federal funds — excess reserves that banks lend to others—indicating some ease in reserve positions during this time. Since the rate at which Federal funds were sold was only slightly below the discount rate during the last half of June, this also indicated that District banks experienced relatively less pressure on their reserve positions than did banks generally throughout the country. In July, however, the situation was reversed, with District banks becoming net buyers of Federal funds.

CHANGES IN SELECTED BALANCE SHEET ITEMS OF WEEKLY REPORTING MEMBER BANKS IN LEADING CITIES

(dollar amounts in millions)

	Twelfth District				United States			
	From May 30, 1962 to July 11, 1962		From July 12, 1961 to July 11, 1962		From May 30, 1962 to July 11, 1962		From July 12, 1961 to July 11, 1962	
	Dollars	Percent	Dollars	Percent	Dollars	Percent	Dollars	Percent
ASSETS:								
Total loans and investments	+356	+ 1.34	+2,496	+10.20	+1,580	+ 1.29	+10,251	+ 9.02
Loans adjusted and investments[1]	+383	+ 1.45	+2,461	+10.14	+1,846	+ 1.53	+10,104	+ 8.99
Loans adjusted[1]	+303	+ 1.80	+1,703	+11.00	+ 892	+ 1.19	+ 5,599	+ 8.01
Commercial and industrial loans	+ 80	+ 1.39	+ 488	+ 9.13	+ 424	+ 1.29	+ 1,729	+ 5.48
Real estate loans	+118	+ 2.05	+ 538	+10.10	+ 332	+ 2.36	+ 1,477	+11.43
Agricultural loans	+ 33	+ 3.88	+ 162	+22.47	+ 6	+ 0.44	+ 223	+19.21
Loans to nonbank financial institutions	+ 30	+ 3.53	+ 116	+15.16	+ 319	+ 5.66	+ 972	+19.51
Loans for purchasing and carrying securities	— 28	—10.41	+ 39	+19.31	— 508	—12.36	— 319	— 8.14
Loans to foreign banks	+ 22	+ 9.21	+ 59	+29.21	+ 77	+11.11	+ 183	+31.18
Other loans	+ 52	+ 1.50	+ 333	+10.44	+ 252	+ 1.43	+ 1,490	+ 9.09
Loans to domestic commercial banks	— 27	—10.47	+ 35	+17.86	— 266	—15.70	+ 147	+11.48
U. S. Government securities	— 2	— 0.03	— 12	— 0.18	— 19	— 0.06	+ 781	+ 2.48
Other securities	+ 82	+ 2.79	+ 770	+34.13	+ 973	+ 7.07	+ 3,724	+33.84
LIABILITIES:								
Demand deposits adjusted	+271	+ 2.37	+ 104	+ 0.90	— 54	— 0.09	— 325	— 0.53
Time deposits	+179	+ 1.23	+1,874	+14.60	+ 771	+ 1.66	+ 7,296	+18.26
Savings accounts	+252	+ 2.24	+1,252	+12.20	+ 766	+ 2.39	+ 4,097	+14.24

[1] Exclusive of loans to domestic commercial banks and after deductions of valuation reserves; individual loan items are shown gross.
Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

Little change in District rates for short-term business borrowing

The June quarterly interest rate survey conducted by the Federal Reserve Bank of San Francisco disclosed an average interest rate (unweighted by loan size) of 5.40 percent on business loans maturing in one year or less made by District banks during the period of June 1-15. This was only 1 basis point above the average rate in the first half of March. The proportion of the total dollar volume of loans made at the prime rate of 4½ percent, however, dropped from 28 percent to nearly 24 percent, as the volume of loans bearing rates of 5 to 6 percent increased. This type of shift occurred in all loan size groups. The average rate on business loans of over one year maturity, which had risen sharply in March to 5.74 percent, declined to 5.40 percent in June, the same average rate as for short-term loans. The decline was partly due to a number of large long-term loans made at or near the prime rate. The rate on long-term loans fluctuates more widely than that for short-term loans. This is due in part to the relatively small number of loans in the former group resulting in the possibility of individual large atypical loans unduly weighting the sample for some survey dates.

Member Banks in Twelfth District Outpace All Others in Postwar Performance

THE "westward movement" which has been one of the characteristics of the postwar period has brought a rate of economic growth to the Twelfth Federal Reserve District in excess of the average for the rest of the nation. Member banks in the District have shared in this growth, and over the postwar period the rate of increase in their total assets has outpaced that of other member banks in the country. Nevertheless, banks in the District reacted in much the same manner as other banks in response to the postwar booms and recessions from October 1949 to April 1958. There were some differences in the magnitude of change and in the relative distribution among loans, investments, and deposits as might be expected to occur as a result of variation in the composition of assets and liabilities, and, possibly, some differences in the timing of cyclical turning points between the District and the rest of the nation. In the last business cycle, however, the differences in the behavior between District and other banks were greater and appear to be of sufficient significance to justify a closer examination of the differences which have existed in the last three cycles and in the present cycle to date.[1] Before comparing cyclical responses, the secular trends in certain bank asset and liability items will be discussed, and some of the historical differences in asset and deposit composition between Twelfth District member banks and all other member banks will be briefly reviewed. The basic period for which the secular trends will be described starts with the business trough in October 1949 and ends with the most recent trough in February 1961, although not all of the data are available as of those exact months.

In the analysis below, the performance of all member banks in the Twelfth District is compared with that of all other member banks, that is, all member banks in the United States minus Twelfth District banks. As the analysis is confined to member banks only, the term "banks" implies "member banks" even though not specifically stated. Nonmember banks which became member banks during the period under review are included in the data as of the date they became members but are not reflected in the data prior to such date. As a result, the composition of the universe changes over time and to this extent comparisons based upon different time periods may be somewhat distorted. However, except for the period February 1961 to date, the dollar amounts involved are relatively small and no adjustments have been made except where specifically mentioned in the text. The banking data used in this study have not been adjusted for seasonal variations. This results in some distortions in comparisons of the magnitude of change in one period with another. However, to the extent that seasonal patterns of District banks and all other banks can be assumed to be similar, comparisons of the behavior of the two groups over the same time period would appear to suffer little distortion as a result of using seasonally unadjusted data.

Population in-migration and industrial expansion stimulated Twelfth District bank growth

In assessing the performance of member banks in the Twelfth District with that of member banks in the rest of the nation during

[1] The reference troughs and peaks used in this article are those applicable to national economic activity as dated by the National Bureau of Economic Research. They are: October 1949 (T), July 1953 (P), August 1954 (T), July 1957 (P), April 1958 (T), May 1960 (P), February 1961 (T).

the postwar period, it is helpful to have some measures of the magnitude of growth in the District relative to that in the rest of the country, such as that provided by census data and personal income figures. Although banks through extension of credit may directly influence business activity, they, in turn, are affected by the economic growth of the area in which they operate. As the natural increase in population was augmented by the large postwar migration to the West, the population of District states (including Hawaii and Alaska) increased 41 percent from 1950 to 1960 in contrast to an increase of only 16 percent in the United States less the Twelfth District states. Since individuals normally transfer their checking and savings accounts when they move from one location to another, this in-migration to District states could be expected to serve as a factor contributing to a high rate of deposit increase at District banks. During the postwar period there was also an influx of capital investment into the District which contributed to the extremely rapid expansion of economic activity in the area. Some measure of this capital flow into the District may be obtained from census data on manufacturing. From 1947 to 1958, the number of manufacturing establishments in District states (excluding Alaska and Hawaii) rose 59 percent and value added by manufacture increased 181 percent. This compares with increases of 21 percent and 82 percent for the rest of the nation. The population growth in the District also stimulated the expansion in retail stores and service trades so that the rate of increase both in number of retail establishments and in sales was greater than in the rest of the nation. As many Eastern firms established plants, distribution centers, and retail outlets in the West, funds were transferred into District states. This development, along with the flow of deposits accompanying the population shift westward, acted as a retarding influence on the rate of deposit growth in the rest of the country, while stimulating deposit growth in the District.

Personal income in the Twelfth District (excluding Alaska and Hawaii) reflected the fast pace of postwar economic activity in the District, registering an increase of 129 percent from 1949 to 1960, a substantially higher rate of change than the 88 percent increase for the remainder of the continental United States. The rate of increase in personal income during this period was large enough to maintain per capita income in the District at approximately the same relationship to the national average as that existing at the beginning of the postwar period, despite the high rate of population growth.

Demand deposits have grown much more rapidly in District than in rest of nation

Viewed against this background, it is not surprising that the growth of banks in the Twelfth District from October 1949 to February 1961 has been more rapid than in the rest of the nation.[1] This is clearly depicted in Table 1 and Charts 1-3. As indicated in the table, the much higher rate of increase in total deposits at District banks was largely due to a percentage increase in demand deposits twice that experienced by other member banks. This development reflects both the disparate rates of population growth between the District and the rest of the country and the rapid expansion in the industrial base of the District. Funds that flowed into the District from transfers of personal deposit accounts and business accounts were augmented by deposits created by the greatly expanded volume of loans extended by banks in the District during this period.

[1] February 1961 data for both District and all other member banks have been adjusted to exclude a sizable transaction with a national retailer involving the net loan and time deposit categories. Adjustments have also been made to exclude asset and liability items of a former large nonmember District bank included in the series for the first time in February 1961.

TABLE 1

PERCENT CHANGE IN LOANS, INVESTMENTS, AND DEPOSITS

October 1949-February 1961[1]

	Twelfth District member banks	All other member banks
Total loans and investments	+ 89	+ 59
Loans, net	+189	+178
Investments	+ 15	— 1
U. S. Government securities	— 1	— 16
Other securities	+118	+102
Total deposits	+ 81	+ 49
Demand	+ 61	+ 33
Time	+113	+106

[1] February data for both District and all other member banks have been adjusted to exclude a transaction with a national retailer involving the net loan and time deposit categories. District member bank data for February have also been adjusted to exclude assets and liabilities of a former large nonmember bank included in the series as of that date.

Source: Board of Governors of the Federal Reserve System; Federal Reserve Bank of San Francisco.

District banks have traditionally had higher percentage of time deposits

As time deposits more than doubled, banks in the District also retained their traditionally higher percentage of time to total deposits than other banks. This historical differential is due to a number of factors. Banks in the District have actively sought savings deposits, and the branch banking systems, characteristic of the District's banking structure, have permitted wide access of large banks to individual depositors, even in smaller communities. In addition, in some District states the absence of enabling legislation for mutual savings banks has removed this source of competition for savings funds. In the late twenties, time deposits at District banks constituted about 53 percent of total deposits, dropping to around 50 percent in the late 1930's, while other member banks had ratios of 37 percent and 25 percent, respectively, for those two periods. In October 1949, 39 percent of total deposits held by Twelfth District member banks were time deposits and by February 1961 the percentage had risen to 45 percent. In the same period the ratio for all other member banks changed from 22 to 30 percent.

This difference in deposit composition has been reflected in the ratio of loans to deposits[1] of District banks. There is no established standard "safe" loan-deposit ratio; over time, bank opinion has changed as to how high the ratio could rise under sound banking practice. Deposit fluctuation is one of the controlling factors and this varies, not only with the business cycle, but by type of bank and by location. Because a larger share of their total deposits consists of less volatile time deposits, banks in the Twelfth District during the postwar period have permitted their loan-deposit ratio to rise higher than the ratios at all other banks except New York City banks, which typically carry a high percentage of loans to deposits.

Expansion in District economy reflected in greater growth in loans

Turning from the liability side of the balance sheet to the asset side, a reference to Table 1 and Charts 1-2 shows that the amount of total credit[2] extended by member banks in both the Twelfth District and the rest of the nation rose secularly from the recession trough of October 1949 to the recent cyclical trough of February 1961. The increase in District bank reserves resulting from the large influx of deposits and the very heavy demand for bank credit engendered by the rapid expansion in economic activity were largely responsible for the approximately one-third higher rate of growth in total credit of District banks than of all other banks. This increase in total credit was concentrated in loan portfolios, which almost tripled at District banks as funds were extended to meet not only credit demands that had accumulated during the war period but also those associated with the expanding District economy.

[1] Loans adjusted (total net loans less loans to banks) to total deposits less cash items in process of collection.

[2] Total net loans (gross loans less valuation reserves) and investments.

This is clearly illustrated in the trend of commercial and industrial loans;[1] such loans increased in dollar volume more than three times from the end of 1949 through December 1960[2] as District banks supplied funds to finance the fast pace of business activity (Table 2). Consumer loans outstanding at District banks also tripled during this period, with the percentage increase being slightly above that for all other banks.

From 1949 through 1960, Twelfth District states accounted for over one-fifth of all new residential housing units in the nation but, paradoxically, the volume of real estate loans held by District banks, although doubling, increased by a smaller percentage than for all other banks. There are a number of factors which serve to explain this behavior. At the beginning of the period, District banks already held a much higher proportion of real estate loans to total loans than other banks. Savings and loan associations in the District had an extremely rapid rate of growth during this period, and outstanding mortgage loans held by insured savings and loan associations in the District increased over eight times, from around $1.3 billion at the end of 1949 to approximately $11.3 billion by the end of 1960, a relatively greater increase than occurred outside the District. In addition, funds

TABLE 2

PERCENT CHANGE IN SELECTED LOAN CATEGORIES

December 31, 1949 - December 31, 1960

Loans	Twelfth District member banks	All other member banks
Commercial and Industrial[1]	+233	+175
Real Estate	+130	+163
Consumer	+235	+229

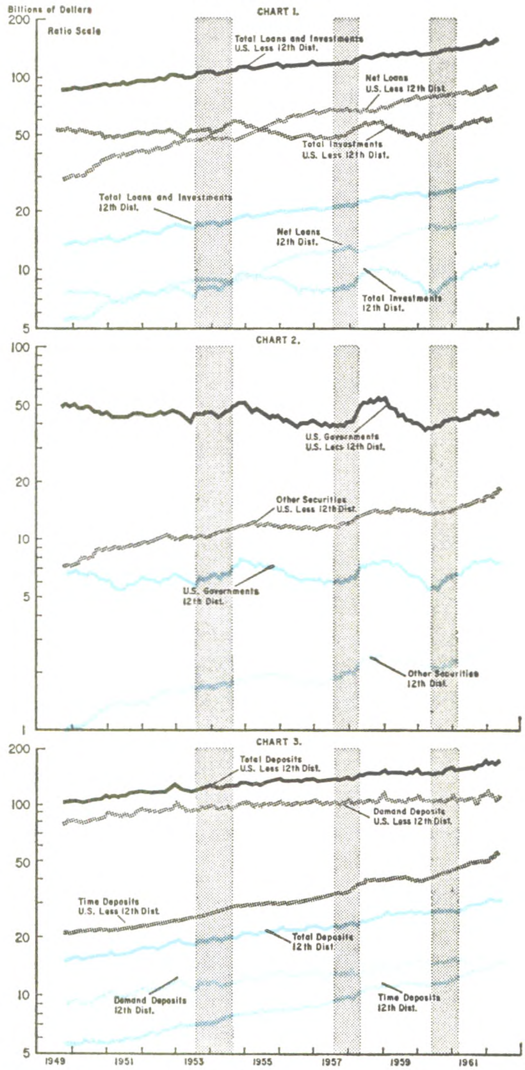
[1] Includes loans to sales finance companies; partially estimated for December 31, 1960.
Source: Member Bank Call Report, Board of Governors of the Federal Reserve System.

CHARTS 1, 2, 3

SELECTED ASSETS AND LIABILITIES OF MEMBER BANKS TWELFTH DISTRICT BANKS AND ALL OTHER BANKS

October 1949 - April 1962

(billions of dollars)



Note: This chart is plotted on a ratio or semi-logarithmetic scale on which equal vertical distances represent equal *percent* changes rather than equal absolute amounts.
No adjustments have been made for changes in the universe of the series during the period covered.
Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

[1] Including loans to sales finance companies; partially estimated for December 1960.
[2] Based on Call Reports of Condition of Member Banks as of December 31, 1949 and December 30, 1960.

available from within the District were supplemented, as in the past, by drawing on savings from outside the District to meet the credit demands of the area. This was particularly true in connection with financing the residential construction boom as Eastern insurance companies acquired large amounts of Twelfth District mortgages. However, notwithstanding the proportionately smaller rate of increase in real estate loans at District banks, one-fourth of the total volume of outstanding real estate loans of all member banks in the nation was held by Twelfth District banks at the end of 1960.

District bank security holdings rose while those of other banks declined

In addition to a higher rate of loan expansion, District banks had a 15 percent increase in total security holdings from October 1949 to February 1961 in contrast to a nominal decline for all other member banks. However, as indicated by Table 1 and Charts 1-2, data on total investments disguise the diverse movements in bank holdings of United States Government securities and of other securities. Both groups of banks entered the postwar period with large holdings of United States Government securities, but over the subsequent period District bank holdings declined 1 percent and holdings of all other banks were reduced 16 percent. In contrast, bank portfolios of other securities more than doubled for both groups of banks as assets with higher rates of return were sought to offset steadily increasing bank expenses. As a result of these divergent movements, the percentage of other securities to total security holdings changed from approximately 13 percent in 1949 to 26 percent in 1961 for both bank groups.

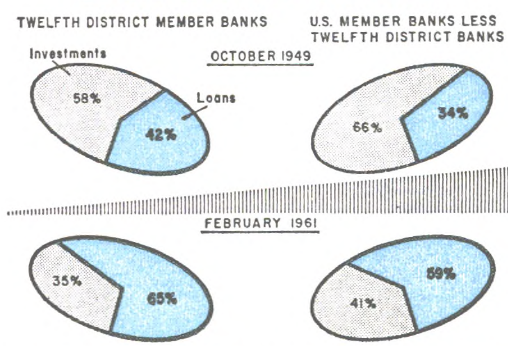
The allocation of total bank credit between loans and investments changed materially over the postwar period, as illustrated in Chart 4. Because of the sizable holdings of United States Government securities accumulated during the war years, both bank groups in October 1949 held a larger volume of securities than of loans, a reversal of the normal pattern. In the following years, funds from sales of Government securities and from issues which were not replaced at maturity were reinvested either in loans, to help meet the strong private demand for bank credit, or in higher paying municipals and other securities. Throughout the 1949-61 period, District banks maintained a higher percentage of total credit in loans than did other member banks. The volume of loans outstanding exceeded security holdings at District banks as early as 1951, while this change did not occur at other banks until 1955 (Chart 1).

District banks rank among largest in nation

To summarize, the secular growth in assets and liabilities of member banks in the nation during the period October 1949 to February 1961 reflects the rapid recovery after the war and the longer run growth in the economy. Several factors contributed to a higher growth rate for banks in the Twelfth District than in the rest of the nation during this period. The large postwar in-migration

CHART 4

CHANGES IN DISTRIBUTION OF MEMBER BANK CREDIT BETWEEN LOANS AND INVESTMENTS



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

of population and the influx of capital investment brought a flow of funds into the District and contributed to an extremely rapid expansion in the economic activity of the area. For District member banks this resulted in a high rate of deposit growth and loan expansion. By the end of 1961 fourteen banks[1] in the San Francisco Federal Reserve District were included among the fifty largest banks in the nation (ranked by deposit size), compared with eleven banks in the New York Reserve District and eight in the Chicago District. A Twelfth District bank ranked in first position and six banks were in the billion dollar deposit size group. The greater number of large banks in the Twelfth District also reflects the fact that the laws of District states permit branch banking on a wider geographic scale than do those of most other states.

The following analysis of the cyclical behavior of banks in the postwar period must be viewed against this background of rapid secular deposit and loan expansion. Any assessment of the response of the banking sector to future cycles also must take into consideration changes which may occur in the pace of secular growth.

Many factors affect banks' response to business cycle

The manner in which banks respond to cyclical movments is based on a number of factors. Actions of the monetary authority determine whether banks as a whole have free reserves with which to expand their loan portfolios or are in a tight reserve position where they tend to restrict new loan commitments in order to avoid reserve deficiencies which necessitate borrowing from the Reserve Bank. Chart 5 shows, for the period under discussion, member bank excess reserves and borrowings from the Federal Reserve Banks. If excess reserves exceed borrowings, the difference is referred to as net "free" reserves; conversely, if borrowings, are greater than excess reserves, the difference is designated as net "borrowed" reserves. When business activity advances at a rapid pace and inflationary pressures mount, the Federal Reserve System normally pursues a restrictive monetary policy, making reserves relatively less available to the banking system. Under these circumstances, member banks as a group typically have net "borrowed" reserves which places them under greater constraint with respect to further credit expansion. During a recession, on the other hand, the System follows a policy of ease and member banks typically have net "free" reserves. This permits the banks to expand loan and investment portfolios and to meet demands for credit which may not have been filled during the upturn in the business cycle.

In addition to the effects of monetary policy, the response of banks to the business cycle is determined by liquidity considerations (such as the ratios of loans to deposits and of short-term securities to deposits), the maturity composition of loan portfolios and of securities portfolios, and the character and type of deposit liabilities. There are also other considerations of a somewhat more intangible type which include bankers' expectations as to the business outlook and the course of interest rates in both the immediate future and the longer term.

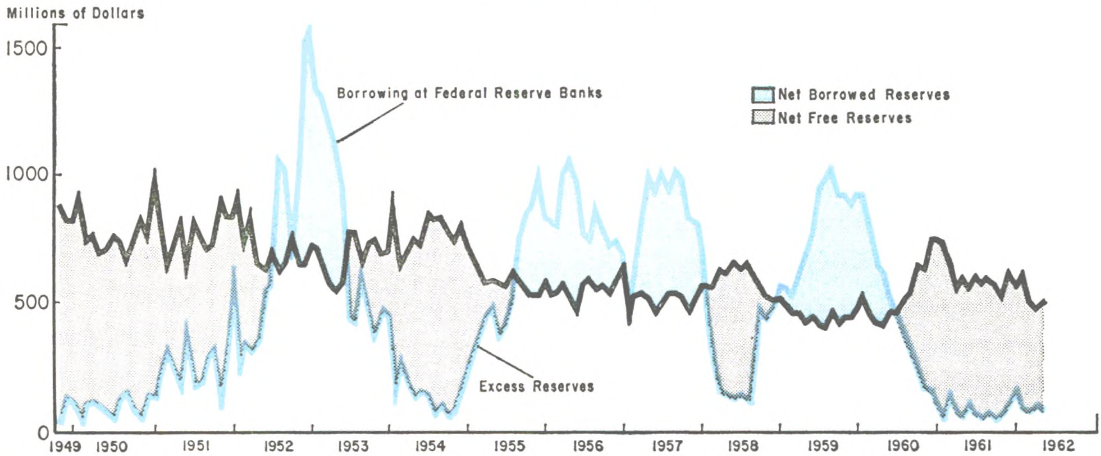
Rate of loan and deposit expansion has declined in each succeeding cycle

As indicated in Chart 6, there has been a declining trend in the rate of loan and deposit expansion over the last three business cycles as the added impetus of war-accumulated demands diminished and the periods of cyclical expansion became progressively shorter. The chart also shows that the spread between the rates of increase of loans and deposits at District banks and at all other banks

[1] Thirteen member banks and one nonmember bank.

CHART 5
CHANGES IN NET RESERVE POSITION OF MEMBER BANKS IN THE UNITED STATES

October 1949 - April 1962



Source: Board of Governors of the Federal Reserve System.

widened in favor of the District in each succeeding cyclical upturn. What are some of the factors that might have contributed to this latter development? The long-term growth in loans and deposits would be expected to increase the upward movement in these items above that which would have resulted from purely cyclical factors, and the higher rate of secular growth at District banks than at other banks could be expected to have a more discernible effect on the rate of expansion in the latter part of the postwar period after war-accumulated demands for credit had been largely removed as an expansionary factor. In addition, personal income data appear to indicate that District states in the latter part of the postwar period widened their lead over the rest of the country in the rate of increase in overall economic activity. Data on nonagricultural employment also indicate that in the first of the postwar cycles under discussion the timing of the cyclical upturn in the District may have lagged that of the nation as a whole, while in the 1958-60 expansion the District appears to have had an earlier and more rapid upturn from the trough than the rest of the country.

District bank performance lagged in 1949-53 cycle

In the first business cycle under consideration, October 1949-July 1953, the greater loan expansion, than in subsequent postwar cycles, is explained by the fact that credit demands unfilled during the war years were still being met, along with new demands arising from the Korean War. Expansion was further stimulated by the relative lack of monetary restraint on bank reserves. Until the Accord of 1951 with the United States Treasury, the Federal Reserve System had been supporting the prices on Government securities. As a consequence, during most of the 1949-1953 cyclical rise, banks could readily dispose of their United States Government securities without incurring capital losses, and until mid-1952 the banking system had net free reserves (Chart 5).

During this cycle the rate of increase in total credit extended by Twelfth District banks fell 6 percentage points below the rate of expansion at all other banks, due to a lower rate of loan increase. As previously mentioned, there is some evidence that the cyclical upturn in the District may not have occurred as early as in the nation as a whole. Loan expansion in the District did not turn up sharply until the eighth month after the trough and the rate of increase remained below 2 percent through the sixth month compared with a rise of nearly 6 percent for all other member banks. For the entire period October 1949-July 1953, both business loans and real estate loans rose proportionately less at District banks.[1] As discussed in the analysis of long-term growth, the already high proportion of real estate to total loans at District banks may account, in part, for the smaller rise in this category. Consumer loans, on the other hand, registered a rate of gain 20 percentage points greater than at other banks, reflecting demands stemming from the large inflow of population to the District.

Foreshadowing the trend in the succeeding cyclical expansions, the 25 percent gain in total deposits at District banks exceeded that for all other member banks by almost 8 percentage points, with both demand and time deposits increasing at high rates. This substantial deposit gain provided funds for loan expansion without the necessity of reducing total security holdings. Despite a 50 percent increase in total net loans, banks in the District had a gain in total investments during this period, in contrast to a small decline nationally. While holdings of United States Government securities were reduced 4 percent (less than half the rate of reduction at all other banks), District banks increased the dollar amount of their other security holdings 61 percent, compared with an increase of 41 percent at other banks.

As mentioned earlier, banks in October 1949 had relatively small loan portfolios and

[1] Based on Call Reports of Condition of Member Banks for December 31, 1949 and June 30, 1953.

unusually low ratios of loans to deposits[1]—the ratio for District banks was 37.9 percent and for other member banks 29.3 percent. The sizable increase in loans in the 1949-53 business boom resulted in a rise of about 10 points in the ratios for both groups of banks. Another gauge of bank liquidity, the ratio of United States Government securities maturing within one year to total deposits less cash items in process of collection also changed. This ratio for District banks declined from 14.0 percent in December 1949 to 11.6 percent in June 1953 and for all other member banks from 13.9 percent to 12.8 percent.[2]

Both bank groups have reacted similarly in recessions

In cyclical downturns banks normally experience a reduction in the volume of outstanding loans or, at least, a sharp decline in the rate of increase prevailing during a cyclical expansion. The strong secular growth in loans during the postwar period has tended to moderate the amount of downward movement during the periods of recession. This was evident in the recession period from July 1953 to August 1954 as all other banks had a nominal 1.1 percent increase in loans and District banks a 0.2 percent decline. For both groups of banks, increases in real estate loans helped to offset the decline in business borrowing. Banks generally used funds available as a result of an easier monetary policy to replenish their portfolios of United States Government securtiies, but the rate of investment was twice as great at District banks. The rate of total deposit gain in the District dropped to under 4 percent, slightly higher than for banks in the rest of the country.

District banks led in 1954-57 boom

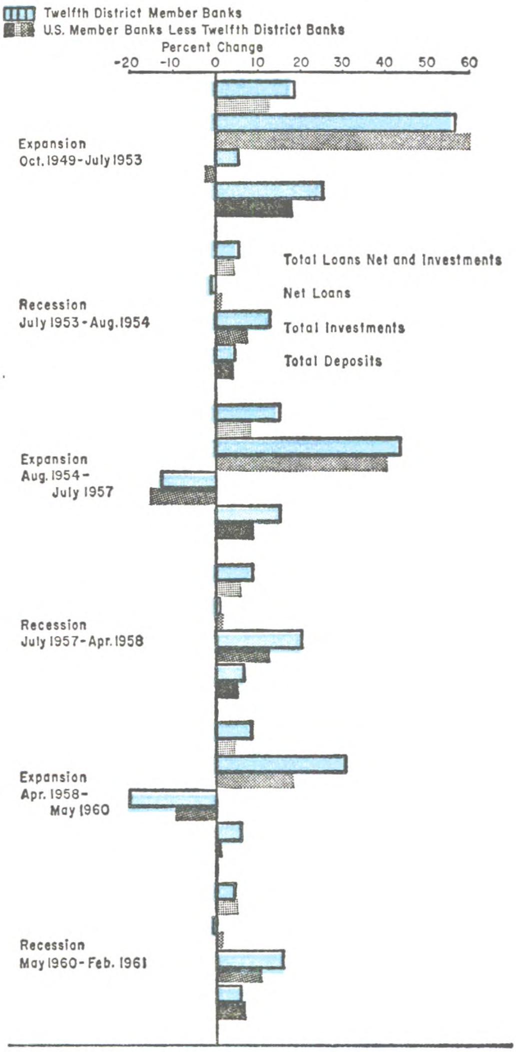
In the succeeding expansion from August 1954 to July 1957, the 15 percent increase

[1] Loans adjusted (net loans less loans to banks) to total deposits less cash items in the process of collection.
[2] Based on partially estimated data.

Chart 6

PERCENT CHANGES IN SELECTED ASSETS AND LIABILITIES OF MEMBER BANKS IN POSTWAR BOOMS AND RECESSIONS

October 1949 - February 1961



Note: February 1961 data for both District and all other member banks have been adjusted to exclude a sizable transaction with a national retailer involving the net loan and time deposit categories. Adjustments have also been made to exclude asset and liability items of a former large nonmember District bank included in the series for the first time in February 1961.
Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

in total credit outstanding at District banks was somewhat greater than in the 1949-53 boom, while the rate of increase at other member banks dropped to 9 percent, only one-half the rate experienced in the preceding upturn. As illustrated in Chart 6, the percentage gains in loans for both groups of banks were less than in the 1949-53 period, but, instead of lagging behind, Twelfth District banks had a slightly higher rate of growth than other banks, largely as a result of a proportionately greater increase in business loans.[1] Banks were faced with a generally tighter reserve position than in the former business cycle and to provide funds for loan expansion they had to reduce their investment portfolios by substantial amounts. District banks reduced their holdings of United States Government securities at a rate four times greater than in the 1949-53 period, but the percentage decline was still less than for other banks. Both groups of banks continued to make small net additions to their holdings of securities other than United States Governments.

Although the rate of increase in total deposits was less than in the preceding cycle, banks in the District widened their favorable margin of deposit growth compared with other banks. This applied to both demand and time deposits. Loan deposit ratios for both groups of banks again moved up—for District banks to 56.1 percent and for all other banks to 51.3 percent. This was accompanied by corresponding declines in the security-deposit ratios to 6.0 percent and 6.8 percent, respectively.

In the downturn of this cycle, July 1957 to April 1958, both groups of banks had only nominal increases in loans. Net additions to security holdings, however, were substantial and, as in the preceding recession,

[1] Based on Call Report of Condition data for June 30, 1954 and June 6, 1957.

the rate of increase at District banks was double that of other banks. Deposit growth in the District also continued at a higher rate. As a result, the loan-deposit ratio at District banks declined more than at other banks, reducing the differential between the two groups to 3.6 percentage points.

Loan expansion widened in favor of District banks in 1958-60

The cyclical upturn which followed the 1957-58 recession was limited to 25 months compared with 45 months and 35 months in the two preceding cycles. In the expansion from April 1958 to May 1960, Twelfth District member banks displayed wider variation from other banks in the rate of loan and deposit growth. Over these two years of rising business activity, the 8.3 percent rate of increase in total bank credit at District banks was one-third greater and the rate of loan increase two-thirds greater than for other member banks.[1] Loan volume rose two months after the trough for both groups of banks, due largely to June tax borrowing, but then the patterns diverged as loans continued to expand at District banks whereas they contracted and remained below the trough level at all other member banks until September 1958. This would appear to lend support to the possibility that the cyclical turning point might have been earlier for the District than the rest of the country and indicates a sharper and more sustained upturn. The more rapid pace at which District business activity accelerated over the cycle as a whole is evidenced by a percentage gain in commercial and industrial loans twice that at other member banks.[2] The percentage gain in consumer loans was also greater by about 7 percent and, in contrast to the two preceding cycles, District banks had a proportionately larger increase in real estate loans.

[1] District data in April 1958 have been adjusted to compensate for a change in the universe of the District bank series resulting from inclusion of Hawaii in the Twelfth District.

[2] Based on Call Report of Condition data for March 4, 1958 and June 15, 1960. Commercial and industrial loans have been adjusted to include loans to sales finance companies.

Competition for savings reduced time deposit expansion at District banks

Reflecting this faster tempo of business activity and the proportionately larger loan expansion in the Twelfth District as well as greater secular growth, total deposits of District banks registered a percentage gain over ten times that of other banks. This favorable differential, however, was entirely due to the growth in demand deposits, which rose more than 7.5 percent, contrasted to a 2 percent decline at other banks. The increase in time deposits during this period slipped to 5 percent, a rate lower than that for other banks. This relatively poor performance by District banks in attracting savings was due to heavy losses of time deposits in the fall of 1959 and early 1960 when savings depositors withdrew funds for investment in savings and loan associations and in United States Government securities, both of which offered substantially higher rates of return at that time. Banks in the rest of the nation also faced this type of competition for savings, but the differential in interest paid on savings in favor of savings and loan associations was relatively large in California and was combined with aggressive competition for savings funds by these associations.

Security-deposit ratio fell as loan-deposit ratio soared to postwar high

The comparatively favorable loan increase at District banks occurred against a background of restrictive monetary policy which resulted in banks having net borrowed reserves during most of the cyclical expansion except for the first eight months. There was, in general, limited supply of funds relative to demand, and interest rates, including those on bank loans, rose sharply during the period. To meet loan demand, District banks reduced their total holdings of securities at a rate more than twice that of other banks and greater than in the two previous cycles when the percentage growth in loans was considerably higher. Also in contrast to the two earlier cycles, other security holdings as well as United States Governments were sold or not replaced at maturity. The sizable reduction in security portfolios was particularly pronounced in holdings of United States Government securities within one year of maturity and, as a consequence, the security-deposit ratio of Twelfth District member banks fell to a low of 1.6 percent, far under the 3.5 percent for other member banks.[1] Some District banks even had temporary difficulties in providing legally prescribed short-term collateral required to cover certain types of deposits.

The drop in the security-deposit ratio was accompanied by a sharp rise in the loan-deposit ratio of District banks. At the peak of the cycle in May 1960, the ratio reached 64.0 percent, a 10 point jump above the April 1958 trough. Since the ratio for other member banks rose to only 57.3 percent, the differential between the two ratios widened to 6.7 points, placing District banks in a comparatively weaker liquidity position. Bank loans in the District, as well as in the nation, continued to increase after the cyclical turning point, and by June 1960 the loan-deposit ratio for District banks reached a peak of 64.3 percent.

Liquidity position rebuilt during 1960-61 recession

Reflecting the mildness of the downturn from May 1960 to February 1961, loan volume at both bank groups was maintained for most of the recession period at approximately the level reached at the cyclical peak, as shown in Chart 1.[2] As monetary policy eased, the reserve position of member banks changed from one of net borrowed reserves in May 1960 to one of almost $700 million in net free reserves at the February 1961 trough. Banks took advantage of this period of relative lack of reserve pressure to replenish their security holdings, particularly their portfolios of short-term Treasuries which had been reduced substantially during the preceding boom. While all other member banks more than doubled their holdings of Treasury issues of one year and under, District banks quadrupled their holdings.[1] As a result of this substantial increase, the security-deposit ratio of District banks rose by December 1960 to a more comfortable level of 5.8 percent. On the other hand, total deposits of District banks failed for the first time in the postwar cycles (both booms and recessions) to rise proportionately more than at other banks. In the case of time deposits, this was partly a reflection of the increasing interest of other member banks in obtaining time and savings deposits which, starting with the recession period of July 1957-April 1958, resulted in a higher rate of increase in such deposits than that experienced by District banks. By February 1961, the loan-deposit ratio of District banks remained above 60 percent (4.7 points above the ratio for other banks), and thus as the present cycle started its upward course District member banks were still in the process of repairing the inroads the last business boom had made in their liquidity position.

Both domestic and balance of payments considerations influence current monetary policy.

The economic background against which the current cycle is taking place differs in a number of respects from the previous postwar pattern. As already noted, the 1960-61 recession was mild, and loan demand in the

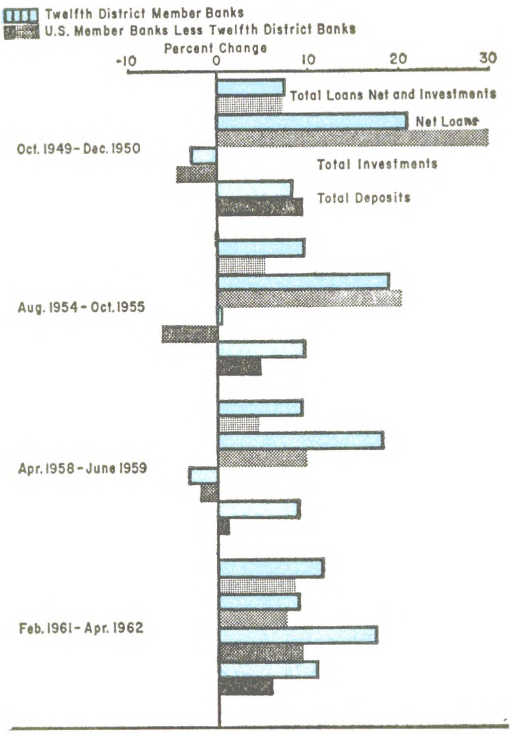
[1] As of June 1960.
[2] Data for February have been adjusted to exclude distortion caused by the inclusion in the series of a nonmember bank as of that date. Adjustments have aslo been made to exclude the effect of a sizable transaction with a national retailer which affected both District and national data for February 1961.

[1] Based on date for June 1960 and Decemebr 1960.

CHART 7

PERCENT CHANGES IN SELECTED ASSETS AND LIABILITIES OF MEMBER BANKS

First 14 months of each postwar recovery



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

succeeding 14 months of expansion was moderate for that stage of the cycle. The threat of inflation which hung over even the early months of expansion of the previous postwar cycles has been relatively absent in the present period, with prices showing a remarkable degree of stability. Under these circumstances, the Federal Reserve System has followed a policy of relative ease in the current expansion in contrast to the noticeable tightening that had occurred in corresponding periods of prior recoveries. Free reserves fluctuated around $500 million through the first 12 months of the present cycle before dropping to around $400 million in the following two months (Chart 5). At the same time, balance of payments considerations have led the Federal Reserve System and the United States Treasury to follow policies that would tend to maintain short-term rates at a level that would discourage outflows of short-term funds; the resultant yields have made it attractive for banks to add to their short-term Government security holdings during this period.

Loans expand relatively slowly in current cycle

As Chart 7 reveals, District banks have had a greater percentage increase in total bank credit during the first 14 months of each postwar business cycle than have all other member banks. In the present cycle, the better performance has been mainly due to the greater growth in security investment rather than in loan expansion. The increase in loans for both groups of banks has been relatively small compared with the first 14 months of the other postwar cycles. The District gain of less than 9 percent is just half that in the corresponding months of the 1958-60 expansion, and a large part of the increase was concentrated late in the fourth quarter of 1961 and in March 1962, both periods of normal seasonal increase in borrowing. The rate of loan increase at District banks in this period was approximately 1 percentage point greater than for other banks. While the percentage increase in commercial and industrial loans was about two and a half times greater, the relative gains in consumer loans and real estate loans were less than for other banks.[1]

The charts on page 155 illustrate the dissimilarity in the loan pattern of this cyclical upturn from that of the former postwar expansions. For the first six months after the February 1961 trough, loan volume fluctuated in a narrow range for both groups of

[1] Information on loan changes by type of loan is based upon Call Report of Condition data for December 31, 1960 (District data adjusted for a change in the universe of the series) and March 26, 1962. Commercial and industrial loan data have been adjusted to include loans to sales finance companies.

banks; then the rate of loan increase at first one group and then the other moved ahead only to reverse positions the following month. This appears to indicate a rough similarity in timing and intensity of the business cycle in the District and the rest of the nation. This differs from the 1949-53 cycle in which, as previously discussed, the all other member bank group clearly set the loan pace in the first 14 months of the boom, and also differs from the 1958-60 upswing when District banks got off to an early lead. It more nearly resembles the closely corresponding movements of District and other member banks in the first 14 months of the 1954-57 period, for then the percentage gain at District banks did not exceed that of other banks until later in the cycle.

Wide divergence from former cycles in pattern of security holdings

Due to relatively easy reserve positions and only moderate loan expansion, both groups of banks made substantial additions to total security holdings in the first 14 months of the current cycle. Reference to the charts on page 156 discloses the wide divergence of this pattern from that of the comparable periods of the other postwar cycles. The 18 percent gain in security holdings at District banks was nearly double that of other member banks, and the change is even more striking in the United States Government securities component, which gained 12 percent at District banks compared with slightly over 4 percent at all other banks. This contrasts with declines in the first 14 months of all the previous postwar cycles. The 33 percent increase for District banks and the 24 percent gain for other banks in holdings of other than United States Government securities is even slightly above the respective increases in the corresponding months of the 1949-53 cycles and, in the case of District banks, contrasts with a decline in the comparable period of the last cycle. The heavy investment by District banks in state and municipal securities in the current expansion is due in large part to their need for earning assets with higher rates of return to meet increased expenses, particularly those arising from higher interest costs on savings deposits. As banks outside the District increased their ratio of time to total deposits, their need for such assets also became more pressing.

Net additions to United States Government securities in the within-one-year maturity category were sufficiently large during this period to raise the security-deposit ratio of District banks to 9.2 percent as of the end of March 1962, compared with a ratio of 11.1 percent for all other member banks.[1] This restored the ratio at District banks to only 1 percent below that prevailing at the beginning of the 1954 cycle and provides a cushion of liquidity with which to meet increases in loan demand which may arise in the future.

Rate of demand deposit growth continues higher at District banks

As in the first 14 months of the two preceding cycles, banks in the District continued to outpace other banks by registering a 10.9 percent gain in total deposits. As in the 1958-60 cycle, however, the more favorable deposit performance of District banks was entirely due to a one-third higher rate of growth in demand deposits; time deposits, although 18 percent above the February 1961 level, fell 2 percentage points behind the increase at other banks. However, the gain in time deposits at District banks was double that in the corresponding period of the 1958-60 cycle and resulted in total time deposits rising to 48.7 percent of all deposits held, whereas for all other banks the ratio of time to total deposits was only 34.3 percent. The charts on pages 154 and 157 indicate the wide variance in the pattern of deposit growth dur-

[1] Data based on the Call Report of Condition of Member Banks for March 26, 1962.

ing the early part of the cyclical periods under discussion.

By April 1962, District banks had pulled their loan-deposit ratio down to 59.7 percent, which compares with a ratio of 56.0 percent for all other member banks. Thus the spread between the ratios, which had increased to 6.7 points at the May 1960 cyclical peak, was narrowed to 3.7. With a much higher security-deposit ratio and a lower loan-deposit ratio, District banks by April 1962 had improved their liquidity position substantially from that at the peak of the 1958-60 boom. As a consequence, they have gained a desirable degree of flexibility which will enable them to more adequately handle future credit demands.

Summary and conclusions

In reviewing the response of District banks to the business cycles in the postwar period certain trends become apparent. As the unfilled demands of the war period were worked off and the economic effects of the Korean War dissipated, the magnitude of the cyclical expansions moderated. The rate of loan and deposit expansion of both District banks and all other member banks reflected this change, becoming progressively smaller in each of the cycles. In the case of District banks, however, the greater secular growth in deposits and loans offset, in part, the moderation of the cyclical upward movement. As a result, the performance of District banks compared with all other member banks became more favorable in each succeeding cycle. The higher percentage increase in total bank credit and deposits at District banks in the first 14 months of the current cycle would appear to indicate that the long-term growth factor will continue to influence the degree of expansion in the present cyclical period.

Until the 1958-60 cycle, the higher rate of deposit expansion at District banks compared with other banks was due to a faster percentage growth rate of both demand and time deposits. However, while the favorable margin of gain in demand deposits has been progressively larger in each cycle since the 1954-57 boom, the increase in time deposits has fallen below that of all other member banks. This pattern has carried over into the current cycle and may be indicative of a basic change in the relative rate of growth in such deposits between the two groups of banks. Since time deposits of District banks now constitute nearly 50 percent of total deposits, a much larger dollar volume than formerly is required to bring about an equivalent percentage increase. In addition, banks outside the Twelfth District have shown an increasing interest in attracting savings and time deposits.

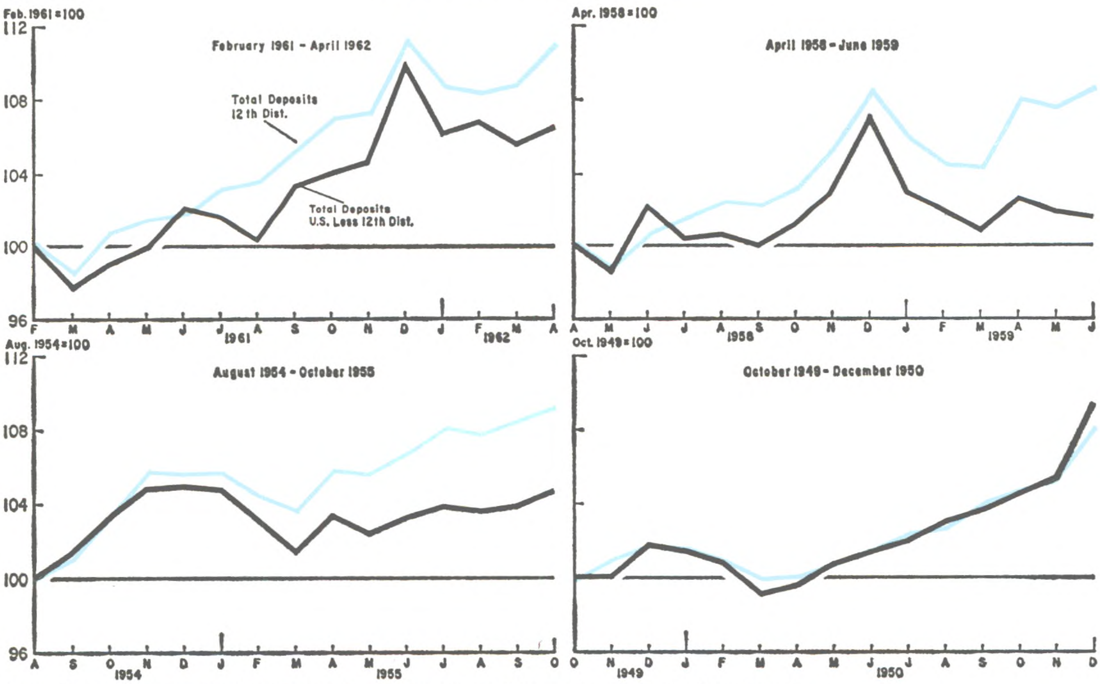
While the more rapid economic growth in the Twelfth District, which resulted from the inflow of business investment and the large population in-migration, produced an expansion of assets and liabilities of District banks in excess of banks in the rest of the nation, it also placed pressures on the banking facilities in the District. Even with their accelerated rate of growth, District banks in the 1958-60 cycle were under some strain in meeting the credit demands generated by the rapidly expanding District economy. This was evidenced by a sharp drop in the security-deposit ratio to 1.6 percent, far below that of other banks, and an increase in the loan-deposit ratio to a high of 64 percent. During the 1960-61 recession and the succeeding upturn, however, District banks rapidly strengthened their liquidity position. By April 1962, the ratio of short-term United States Government securities to deposits was restored to 9.1 percent, approximately the ratio existing at the beginning of the 1954 cycle. Although the loan-deposit ratio remained near 60 percent, the increase in the proportion of time deposits to total deposits, by reducing the volatility of total deposits, enabled District banks to more easily carry a higher loan-deposit ratio.

At the end of March 1962[1] District member banks held 16.7 percent of total loans and investments of all member banks in the nation and 16.6 percent of total deposits. There was a gain of 1 percentage point from October 1949 in the proportion of total net loans of all member banks held by District banks and an increase of 2.8 percentage points in the proportion of total securities held. As of March 1962, District banks accounted for 15 percent of both United States Government security and other security holdings. The gain in District banks' holdings of total deposits over this period was 3.2 percentage points as District demand deposits rose from 10.8 percent to 13.4 percent of the total for all member banks and time deposits from 21.4 to 22.3 percent. This postwar growth in the assets and liabilities of District banks has been reflected in the increasingly important role these banks play in the national money and credit markets. Thus, the secular rate of growth of District banks and their response to cyclical movements have now a greater influence on national credit developments.

[1] Based on the Call Report of Condition of Member Banks for March 26, 1962.

DEPOSIT PATTERN OF MEMBER BANKS DIFFERED FROM ONE RECOVERY TO ANOTHER

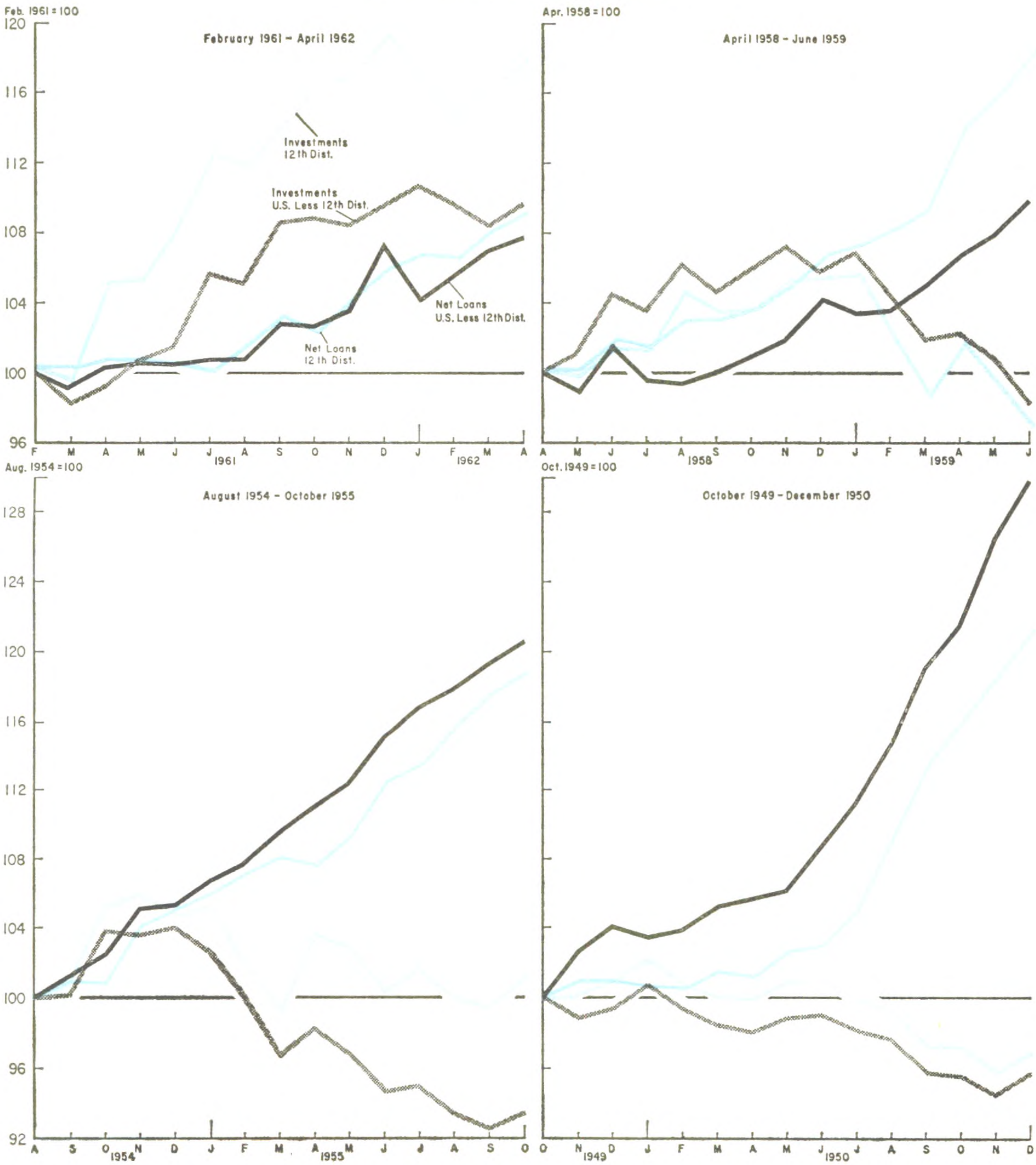
First 14 months of each postwar recovery



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

NET LOAN AND INVESTMENT PATTERN OF MEMBER BANKS DIFFERED FROM ONE RECOVERY TO ANOTHER

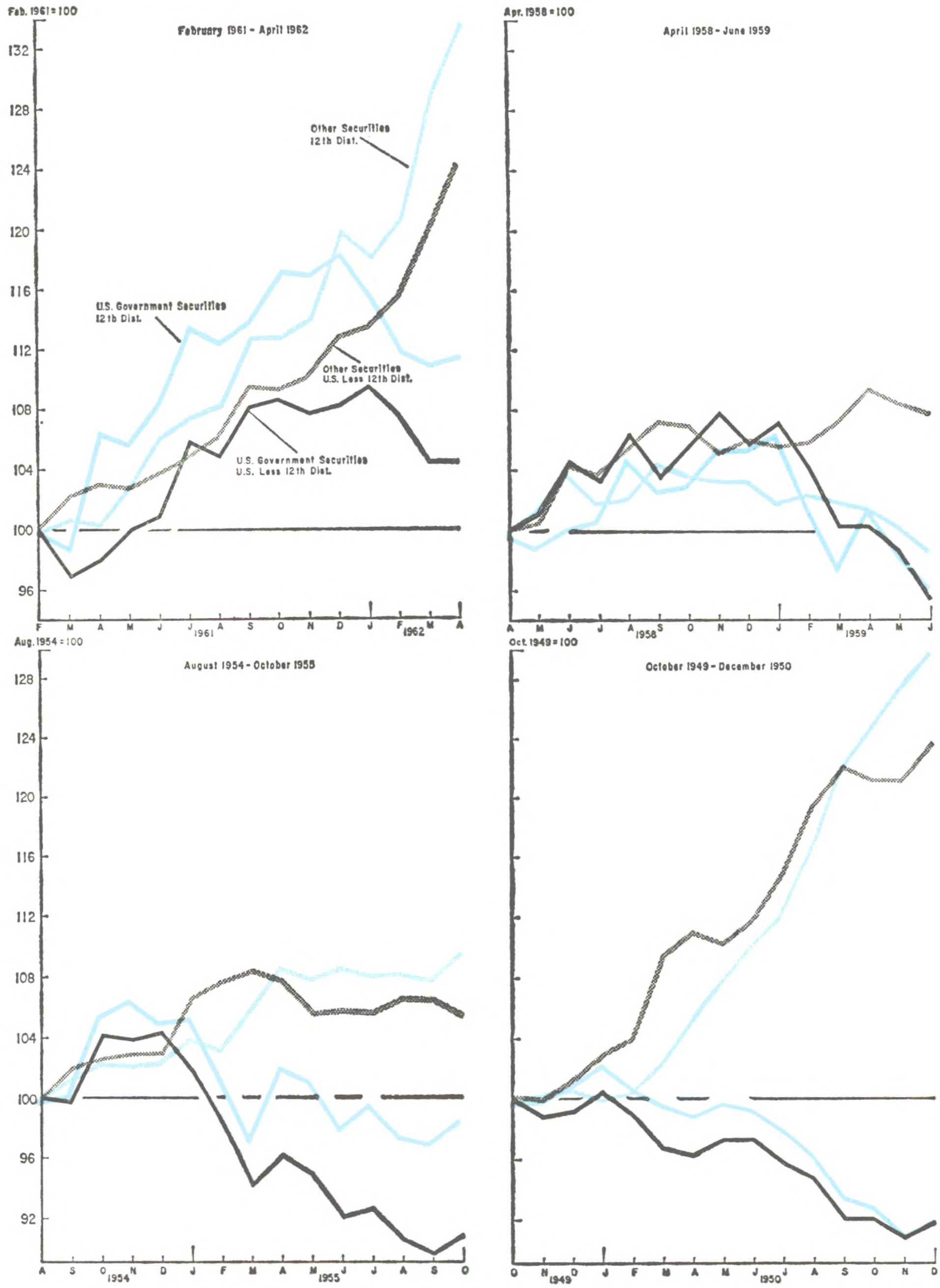
First 14 months of each postwar recovery



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

PATTERN OF SECURITY HOLDINGS OF MEMBER BANKS DIFFERED FROM ONE RECOVERY TO ANOTHER

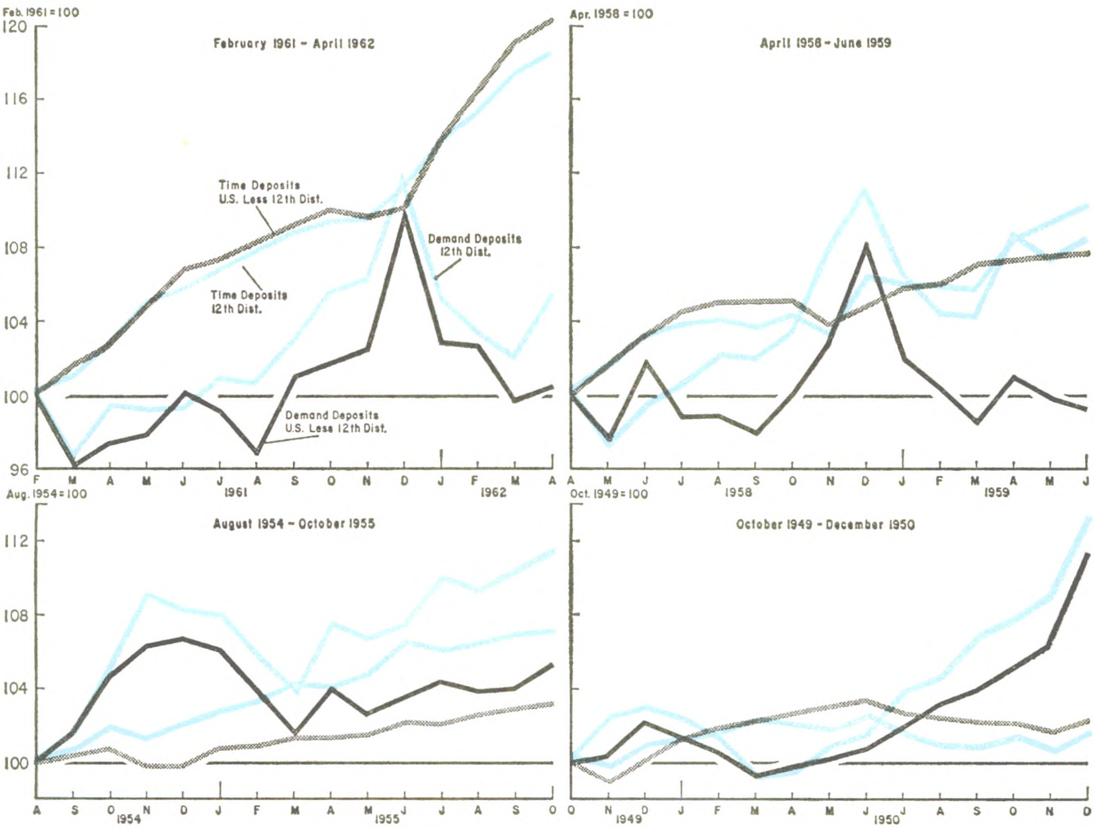
First 14 months of each postwar recovery



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco.

CHANGES IN DEPOSIT COMPOSITION OF MEMBER BANKS DIFFERED FROM ONE RECOVERY TO ANOTHER

First 14 months of each postwar recovery



Source: Board of Governors of the Federal Reserve System and Federal Reserve Bank of San Francisco

REVISION OF DEPARTMENT STORE SALES AND STOCKS INDEXES

As part of the Federal Reserve System's revision of department store sales and stocks indexes, this Bank has prepared revisions from 1947 to date. As these indexes are based on samples, periodically the levels of the series are checked by comparing the change in the sample with the change in Census of Business benchmarks. The current revision includes an adjustment to 1958 Census of Business benchmark data. The indexes have also been recalculated on a 1957-1959 base to reflect more clearly recent developments in department store trade. The third feature of the revision was a review of seasonal factors since 1955 including a re-examination of the special adjustments made in the sales index for the months of March and April to take account of the changing date of Easter.

Revised indexes from 1947 to date are available on request from this Bank. In addition to the revised indexes, factors for converting indexes prior to 1947 to the new base will be furnished.

BANKING AND CREDIT STATISTICS AND BUSINESS INDEXES—TWELFTH DISTRICT[1]

(Indexes: 1947-1949=100, except where otherwise indicated. Dollar amounts in millions of dollars)

Year and Month	Condition items of all member banks[2, 7] Loans and discounts	U.S. Gov't securities	Demand deposits adjusted[3]	Total time deposits	Bank debits index 31 cities[4, 5]	Bank rates on short-term business loans[6, 7]	Total nonagri-cultural employ-ment[11]	Total mf'g employ-ment[11]	Car-loadings (number)[5, 11]	Dep't store sales (value)[5, 11]	Retail food prices[7, 8]
1929	2,239	495	1,234	1,790	42	....	...	...	109	18	64
1933	1,486	720	951	1,609	18	....	...	...	59	11	42
1939	1,967	1,450	1,983	2,267	30	....	...	...	87	19	47
1952	8,839	6,619	10,520	7,502	140	3.95	84	82	108	73	115
1953	9,220	6,639	10,515	7,997	150	4.14	86	86	108	74	113
1954	9,418	7,942	11,196	8,699	153	4.09	85	84	103	74	113
1955	11,124	7,239	11,864	9,120	173	4.10	90	90	112	82	112
1956	12,613	6,452	12,169	9,424	190	4.50	95	96	112	91	114
1957	13,178	6,619	11,870	10,679	204	4.97	98	101	103	93	118
1958	13,812	8,003	12,729	12,077	209	4.88	98	96	96	98	123
1959	16,537	6,673	13,375	12,452	237	5.36	104	103	101	109	123
1960	17,139	6,964	13,060	13,034	253	5.62	106	103	95	110	125
1961	18,499	8,278	14,163	15,116	270	5.46	108	102	94	115	127
1961											
June	17,578	7,571	12,935	14,371	268	5.50	107	102	92r	114	127
July	17,504	7,935	13,206	14,492	267	....	108	102	93r	115	126
August	17,779	7,863	13,212	14,656	262	....	108	103	93r	113	126
September	18,028	7,955	13,317	14,786	277	5.45	108	103	95r	118	125
October	17,901	8,190	13,901	14,867	291	....	109	104	100r	115	126
November	18,212	8,182	13,944	14,874	265	....	109	105	102r	118	127
December	18,499	8,278	14,163	15,116	293	5.42	109	105	104r	120	126
1962											
January	18,646	8,082	13,671	15,448	294	....	110	106	107r	119	127
February	18,622	7,820	13,163	15,647	289	....	110	106	106r	120	128
March	18,906	7,776	13,235	15,939	301	5.50	111	106	104r	123	128
April	19,070	7,811	13,706	16,091	312	....	111	107	104r	118	128
May	19,328	7,582	13,945	16,352	306	....	111	106	99	121	128
June	19,625	7,689	13,101	16,511	315	5.52	111p	106p	100	123	129

Year and month	Industrial production (physical volume)[5] Lumber	Petroleum[7] Crude	Petroleum[7] Refined	Cement	Steel[7]	Copper[7]	Electric power	Waterborne Foreign Trade Index[7, 9, 10] Exports Total	Exports Dry Cargo	Exports Tanker	Imports Total	Imports Dry Cargo	Imports Tanker
1929	95	87	78	55	...	103	29	190	150	247	124	128	7
1933	40	52	50	27	...	17	26	110	...	...	72	...	...
1939	71	67	63	56	24	80	40	163	107	243	95	97	57
1951	113	106	112	128	146	116	136	186	194	175	162	140	733
1952	115	107	116	124	139	115	145	171	201	130	204	141	1,836
1953	116	109	122	131	158	113	162	141	138	145	314	163	4,239
1954	115	106	119	133	128	103	172	133	141	123	268	166	2,912
1955	122	106	124	145	154	120	192	166	178	149	314	187	3,614
1956	120	105	129	156	163	131	209	201	261	117	459	201	7,180
1957	106	101	132	149	172	130	224	231	308	123	582	216	10,109
1958	107	94	124	158	142	116	229	176	212	123	564	221	9,504
1959	116	92	130	174	138	99	252	188	223	138	686	263	11,699
1960	110	91	134	161	154	129	271	241	305	149	808	269	14,209
1961	109	92	140	169	171	136	...	...	...	...	...	...	...
1961													
May	111	92	143	169	191	143	285	265	331	171	865	292	15,856
June	111	91	143	188	187	143	289	224	290	128	767	289	13,223
July	110	91	143	157	183	124	293	271	365	138	1,026	297	20,025
August	111	91	140	160	180	107	300	247	322	140	805	277	14,586
September	111	92	142	163	174	138	295	217	317	76	841	277	15,542
October	110	92	144	171	181	149	310	209	310	67	872	307	15,613
November	113	92	144	182	167	147	305	256	331	148	756	264	13,573
December	106	92	141	152	167	145	294	273	371	134	725	272	12,529
1962													
January	105	90	139	165	184	142	310	245	325	130	762	259	13,870
February	112	92	142r	153	187	158	...	272	353	157	572	249	8,993
March	...	90	137r	175	175	150	...	...	...	...	...	...	...
April	...	90r	135r	192	151	162	...	...	...	...	...	...	...
May	...	91	139	...	161	...	...	...	...	...	...	...	...

[1] Adjusted for seasonal variation, except where indicated. Except for banking and credit and department store statistics, all indexes are based upon data from outside sources, as follows: lumber, National Lumber Manufacturers' Association, West Coast Lumberman's Association, and Western Pine Association; petroleum, cement, and copper, U.S. Bureau of Mines; steel, U.S. Department of Commerce and American Iron and Steel Institute; electric power, Federal Power Commission; nonagricultural and manufacturing employment, U.S. Bureau of Labor Statistics and cooperating state agencies; retail food prices, U.S. Bureau of Labor Statistics; carloadings, various railroads and railroad associations; and foreign trade, U.S. Department of Commerce. [2] Annual figures are as of end of year, monthly figures as of last Wednesday in month. [3] Demand deposits, excluding interbank and U.S. Government deposits, less cash items in process of collection. Monthly data partly estimated. [4] Debits to total deposits except interbank prior to 1942. Debits to demand deposits except U.S. Government and interbank deposits from 1942. [5] Daily average. [6] Average rates on loans made in five major cities, weighted by loan size category. [7] Not adjusted for seasonal variation. [8] Los Angeles, San Francisco, and Seattle indexes combined. [9] Commercial cargo only, in physical volume, for the Pacific Coast customs districts plus Alaska and Hawaii; starting with July 1950, "special category" exports are excluded because of security reasons. [10] Alaska and Hawaii are included in indexes beginning in 1950. [11] Index: 1957-1959=100. p—Preliminary. r—Revised.