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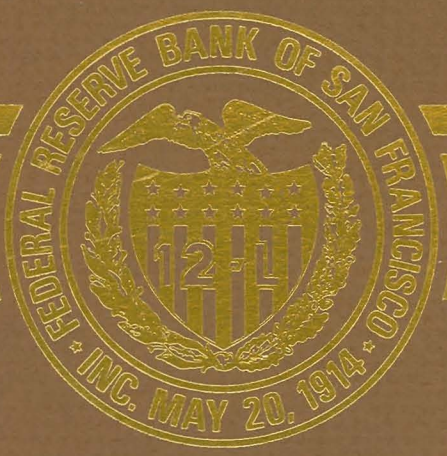
1979

Annual Report

Federal Reserve Bank of San Francisco



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Joseph F. Alibrandi
Chairman (1979)

John J. Balles
President

Cornell C. Maier
Chairman (1980)

FROM THE BOARDROOM

The final year of the 1970's was a fitting climax to an unsatisfactory decade, with a mixed report card of pluses and minuses. The national economy expanded by more than 2 percent during 1979, but production weakened in several key industries such as housing and autos. Employment continued to advance steadily, with a record 59½ percent of the adult population working in paid employment, yet the productivity of that labor force actually declined. The price situation meanwhile worsened, climaxing the most inflationary peacetime decade in the nation's history, and in the process continued to undermine the strength of the dollar in overseas markets.

Financial markets in 1979 reflected the strains of the inflation-wracked business expansion. Credit generally remained available, even though more expensive, with $489 billion (annual rate) raised in the markets during the first three quarters of the year. But credit became increasingly costly as interest rates soared to record levels, reflecting tighter policy measures as well as widespread inflation expectations. For example, banks' prime business-lending rate rose by four percentage points for the second year in a row, reaching a late-fall peak of 15¾ percent before declining to 15 percent at many banks at year-end.

The Federal Reserve acted aggressively to curb domestic inflation and to stem the decline in the international value of the dollar, especially in an historic policy package adopted on October 6. At that time, the Fed raised its discount rate on member-bank borrowings a full percentage point to 12 percent, imposed a marginal reserve requirement on increases in the aggregate total of certain sources of bank funds—and above all, fundamentally changed monetary-control procedures so that the principal focus was on control of bank reserves and monetary growth. Interest rates were permitted to fluctuate over a much wider range, in contrast to the former practice of pegging the Federal-funds rate governing interbank borrowing. These Federal Reserve actions, plus higher interest rates, contributed to a marked slowdown in the growth of the money supply in the final quarter of 1979, as a necessary first step in efforts to slow the pace of inflation.

The $345-billion regional economy served by the Federal Reserve Bank of San Francisco expanded at a much faster rate than the rest of the country, following a pattern set early in the decade. For example, Western commercial banks outpaced other banks with a 14-percent gain in loans and investments, to a year-end total of $170 billion. Real-estate and consumer loan demand continued almost unabated throughout the year, and business loans showed considerable strength for three quarters before weakening towards year-end.

The San Francisco Reserve Bank met the needs of a growing Western economy by providing an expanded amount of Reserve Bank services during 1979. The Bank's personnel continued to handle massive amounts of checks, coin, and currency, but electronic payments grew spectacularly during the year. While check-processing activity increased 6 percent, wire funds transfers increased 23 percent, and automated-clearinghouse and government-deposit activity jumped 44 percent.

As for the bottom line, the San Francisco Reserve Bank continued to rank among the top two Reserve banks in the cost effectiveness of operations, with an aggregate unit cost 9 percent below the System average. Productivity in these operational activities has increased 65 percent since 1974, following the Bank's development of a major program of productivity improvement. But we realize that future productivity gains will depend heavily on the provision of up-to-date equipment and facilities. Thus, we are breaking ground this year for a San Francisco headquarters building which will replace obsolete facilities constructed more than a half-century ago.

Management benefited greatly during 1979 from the broad-based experience and judgment of the Bank's directors at Head Office and four branches. The directors not only provided guidance on major management decisions and planning goals, but also supplied key information on economic and financial conditions as a support to the Federal Reserve's formulation of monetary policy. Today, 37 public-spirited men and women serve as directors, representing a great variety of economic interests and non-profit organizations from every area of the West.

We are grateful to these individuals, and also to those who completed terms as directors during 1979. We owe an immense debt of gratitude to Joseph F. Alibrandi (President, Whittaker Corporation), who showed great gifts of leadership and motivation during his just-completed term as Chairman of our Board of Directors. Our heartfelt thanks also go to several other individuals who completed tours as directors: Dorothy Wright Nelson (Dean and Professor of Law, University of Southern California Law Center) at our San Francisco office; and Fern Jellison (General Manager of the Social Services Department, City of Los Angeles) and Joseph J. Pinola (Chairman and Chief Executive Officer, Western Bancorporation) at Los Angeles. Finally, we wish to express our appreciation to our officers and staff, whose dedication to the efficiency of Bank operations has enabled us to improve our services continually to the financial community and to the general public.

Cornell C. Maier
Chairman of the Board

John J. Balles
President

February 1, 1980

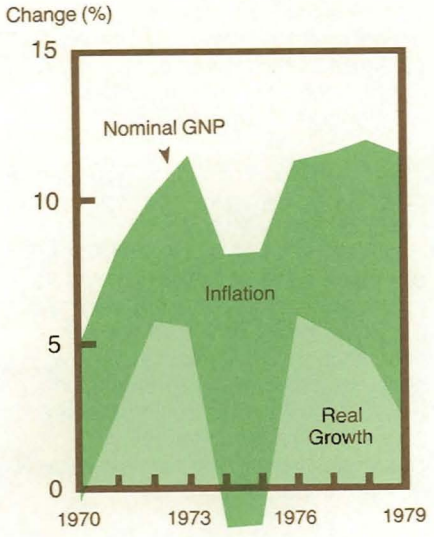
NATIONAL SCENE

The decade of the 1970's experienced some notable achievements and some even more notable failures. On the positive side, the national economy grew 32 percent (in real terms) between 1969 and 1979—a substantial gain, even though it failed to match the 50-percent gain of the preceding decade. Again, real disposable per capita income—a key measure of individual well-being—increased 28 percent in the 1970's, or almost as much as it did in the 1960's. But the nation ate up much of its seed corn in reaching its higher standard of living. Real business investment increased only one-third as fast, and worker productivity less than half as fast, as in the preceding decade. Worse still, the nation became increasingly dependent for its raw materials on unstable and expensive sources of supply, as evidenced by a 15-fold rise in the price of Middle Eastern oil over the decade.

Heavy demand stimulus came from the public sector during the 1970's, as massive Federal spending increases outpaced tax revenues and created red ink on the books for every single year of the decade. Indeed, the combined Federal deficit for the decade, $315 billion, matched the combined total for the entire earlier history of the Republic. Inflation became an ever-worsening problem, reflecting this prolonged series of deficits, the stimulative monetary expansion that sometimes accommodated them, and a series of supply-related shocks. Consumer prices practically doubled over the course of the decade, in the worst peacetime inflation in the nation's history. The accelerating inflation in turn led to a decline in the power of the once-mighty dollar in the world's financial markets.

The year just past typified the decade, with some significant achievements overshadowed by a generally uneven overall performance. Technically speaking, 1979 could not be called a recession year, because employment, income and real output all increased during the period. At the same time, the pace of business definitely slowed, and some major industries suffered substantially. Even worse, inflation accelerated further, aggravated by the soaring price of energy and the continued weakness of the dollar against at least several major currencies.

Real Growth and Inflation



The national economy produced $2.4 trillion worth of goods and services in 1979, as a second-quarter decline in real output failed to offset at least modest gains in each of the other quarters. Real GNP increased 2.3 percent—considerably below the preceding year's 4.4-percent gain, which was more in line with the economy's long-run potential. Yet the level of output maintained in 1979 represented effective full employment, measured in terms of available reserves of experienced workers and cost-effective plant capacity.

SOURCES OF DEMAND

Consumer spending decelerated during 1979, after serving earlier as the mainstay of the four-year-long business expansion. Household disposable income (in real terms) increased 2.2 percent—considerably below the 1978 gain—and even that increase largely reflected an expansion of employment. Despite continued heavy reliance on debt financing, consumer purchases of big-ticket items actually declined (in real terms) as the year progressed, and the 1980-model auto year opened on a notably sour note. Residential-housing activity weakened, with a 14.8-percent decline in housing starts, but the drop was less than might have been expected in view of soaring home prices, record mortgage rates, and a diminished availability of mortgage money.

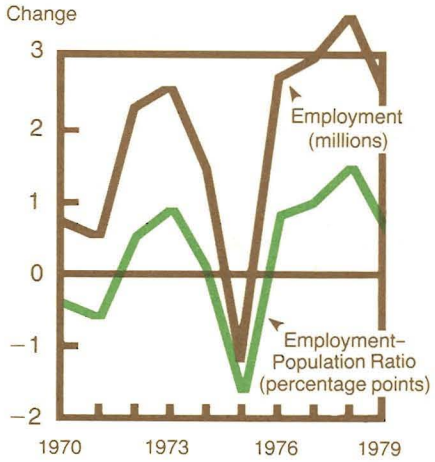
Business fixed investment (in real terms) continued to advance at a relatively strong 5.8-percent pace, offsetting at least part of the decided weakness earlier in the decade. Prior to 1978, investment spending had been concentrated in short-lived equipment (especially trucks and autos), but in the 1978-79 period the emphasis shifted to construction projects (especially factories and commercial buildings). While continuing to show

increased confidence in the future through this investment in long-lived projects, business firms exhibited caution about the near-term outlook by holding their inventories firmly in check, although with some notable exceptions. Export sales represented the strongest single element in the 1979 picture, rising 10.0 percent in real terms as the earlier depreciation in the dollar's value opened overseas markets to many U.S. producers. In contrast, government spending flattened out in real terms, reflecting in part the impact of a nationwide tax revolt.

JOBS, PRICES AND THE DOLLAR

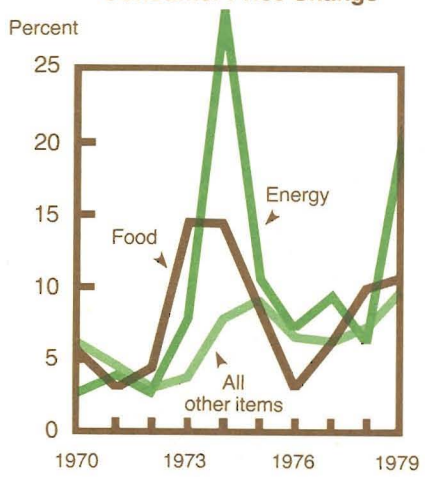
A slowdown in the economy was accompanied by a slowdown in the previous headlong pace of job expansion. Still, employment increased by a respectable 2.5 million in 1979, which altogether meant a 13.5-million expansion in jobs since the early-1975 cyclical trough. Thus, by mid-1979, an unprecedented 59.4 percent of the working-age population was on somebody's payroll. The unemployment rate was relatively stable, averaging 5.8 percent of the civilian labor force for the year. Moreover, experienced workers remained in short supply; the jobless rate for household heads, who comprise the core of the labor force, declined to a very low 3.6 percent.

Change in Employment



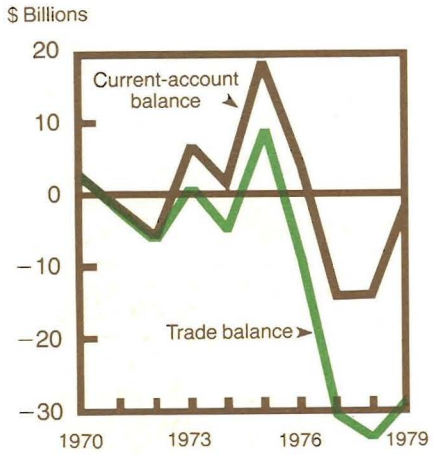
A severe inflation continued to undermine the business expansion, climaxing one of the worst inflationary episodes in the nation's history. The GNP price index (deflator), the broadest measure of price change, rose 8.8 percent after a 7.3-percent increase in the preceding year. The consumer price index rose even faster — indeed, increased 13.3 percent between year-end 1978 and year-end 1979—although that index overstated the actual price rise for such reasons as an overweighting of home-mortgage costs, which affect only a limited number of households. Basically, the worsening of the inflation problem reflected in part the continuation of heavy Federal deficit financing as well as the related difficulty of reducing money-supply growth to levels compatible with the achievement of long-run price stability. But several other factors aggravated the price upsurge. In 1979 as in 1978, early-year farm disasters pushed food prices skyward, while a depreciated dollar made foreign products more expensive. Wage-push inflation worsened because of a near-record 10.2-percent jump in the private sector's unit labor costs, brought about by declining productivity in the face of substantial increases in labor compensation. Most dramatically, the price of the OPEC oil upon which the nation increasingly depends practically doubled over the year, and the effects were soon felt throughout the economy.

Consumer Price Change



The nation's international accounts improved considerably in 1979. Burgeoning foreign demand for U.S. goods, sparked by a cheaper dollar, offset much of the rising bill for imported oil, while income on earlier foreign investments soared in response to the increased value of many foreign currencies. Consequently, the deficit on current account dropped from a massive $13.5 billion in 1978 to practically zero in the first three quarters of 1979. Nonetheless, the world's financial markets moved from crisis to crisis during the year, with inflation fears and the Iranian revolution leading many market participants to flee from many currencies —not simply the dollar—and to buy gold and silver instead. (Gold more than doubled and silver more than quadrupled in price over the year.) Policymakers saw the basic problem as the acceleration of inflation at home and abroad, so the Federal Reserve moved decisively on October 6 to bring that situation under better control.

Balance of Payments



MONETARY POLICY DEVELOPMENTS

Restrictive monetary-policy actions early in 1979—including several boosts in the discount rate (from 9½ to 11 percent)—had failed to stem the rapid growth of the money supply and of the inflation indexes. Hence the Federal Reserve unveiled a three-part policy package on October 6: 1) increasing the discount rate on member-bank borrowings a full percentage point, to a record 12 percent; 2) imposing an 8-percent reserve requirement on increases in the aggregate total of certain "managed liabilities," such as large negotiable time certificates (CD's) and Eurodollar borrowings, and 3) making a fundamental change in the System's monetary-control procedures to focus on controlling bank reserves, rather than on pegging the Federal-funds rate governing interbank borrowing.

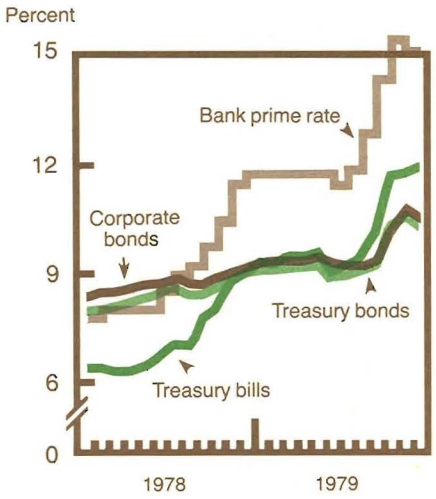
These actions helped produce a significantly slower growth in the money supply and bank credit during the fourth quarter—and also a greater volatility in money-market rates before market participants accustomed themselves to a new and unfamiliar operating environment. With the fourth-quarter deceleration, the annual growth of the narrow M_1 money supply (currency plus bank demand deposits) fell within the 3-6 percent target growth range announced by the Fed early in the year. (This figure adjusts for the impact on demand-deposit growth of automatic transfer-from-savings accounts.) The growth of the broader M_2 measure (currency plus all bank deposits except large CD's) came in slightly above the upper end of the Fed's 5-8 percent target range after being considerably higher during most of the year.

FINANCIAL GROWTH

Net funds raised in 1979's financial markets roughly matched the 1978 total, according to preliminary estimates, as private-sector borrowing offset a decline in debt financing by the public sector. Although Treasury debt increased only half as fast as in 1978, foreign holders liquidated substantial amounts of government securities, forcing the Treasury to rely more heavily on domestic purchasers to finance its debt offerings. State-and-local governments showed modest increases in borrowing and spending. In contrast, Federally sponsored agencies boosted their debt by record amounts, primarily in order to provide support for the weakening mortgage-finance industry. In the private sector, corporate long-term debt expanded at about the 1978 pace, but corporate short-term debt rose faster as firms increased their reliance on bank credit and doubled their sales of open-market paper.

Although funds remained available, they also became more costly. Short-term interest rates were three percentage points higher at the end than at the beginning of the year, under the impact of accelerating inflation, energy shocks, and a tighter Federal Reserve policy. Rate movements also at times became very volatile. Money-market rates began climbing at midyear as business activity and inflation quickened, then shot upward after the October 6 policy package, and finally eased in November and December as the markets learned how to operate in the new policy environment. October's record rates on large CD's, Federal funds and commercial paper prompted banks to hike their prime business-loan rate to a record 15¾ percent, but they later reduced that rate to 15 or 15¼ percent as their cost of funds began to decline. In contrast, Treasury-bill rates lagged considerably behind other money-market rates.

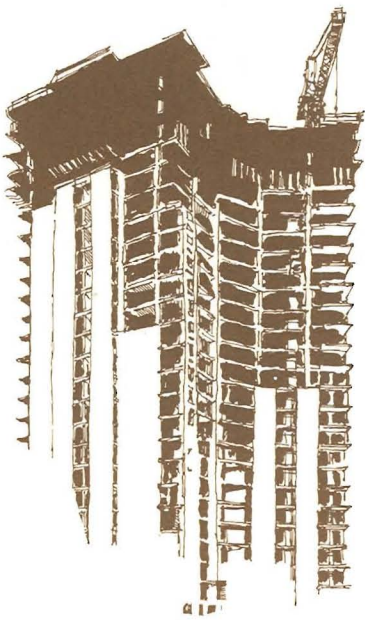
Interest Rates



Long-term corporate bond rates rose modestly in the first half, accelerated during the summer as inflation expectations worsened, and then rose even faster in the fall months as fears surfaced about declining credit availability. Throughout the year, the yield curve retained an inverted shape, with higher yields on short- and intermediate-term maturities than on long-term issues, as is typical of such inflation periods. Prime mortgage rates rose steadily over most of the year, except in states with restrictive usury laws; in late fall they reached a record 14-percent rate in some areas, exerting a dampening impact on housing activity.

BANK CREDIT EXPANSION

Commercial-bank credit expanded by 11½ percent, slightly behind the 1978 pace. Loans accounted for 84 percent of the total increase—down from the preceding year's 90-percent share—as banks built up their liquidity by adding to their holdings of Federal-agency and tax-exempt securities while maintaining their Treasury securities at the 1978 level. Business use of bank credit accelerated to a 17-percent rate, with the borrowing pace at major money-center banks far exceeding that of small banks in the six months prior to October 6. Corporate needs for working capital and for increasingly expensive inventories expanded during the relatively strong first and third quarters, declined during the weak second quarter, and then fell sharply as monetary policy tightened in the fourth quarter of the year. In contrast, bank mortgage lending continued strong throughout 1979, although lagging behind the phenomenal 1977-78 pace. The steep late-year rise in mortgage rates could have been expected to dampen activity in this area, but it came too late to affect 1979 data, because of the long time lag between mortgage commitments and actual loan take-downs. Consumer borrowing meanwhile remained strong until about midyear, but the pace slackened thereafter as consumers, as well as lenders, became more cautious in response to rising consumer-debt ratios and recession fears.



To finance this credit expansion, banks relied more heavily on time deposits (except passbook savings) than on demand deposits. Money-market certificates (MMC's), with their rates tied to Treasury-bill rates, were the most noteworthy source of funds. MMC's quadrupled in volume during the year, offsetting an outflow in fixed-ceiling savings deposits. Issuance of large negotiable CD's declined slightly during 1979—unlike 1978 and other recent periods of high interest rates—because banks could obtain funds more cheaply through money-market certificates and some non-deposit sources such as Eurodollars.

RISING BANK EARNINGS

Bank income reached a new peak in 1979, according to preliminary data for the year. Operating earnings increased, as banks expanded their volume of earning assets and benefited from soaring rates of return on those assets—for example, with the rise in the prime business-loan rate from a midyear level of 11½ percent to a fall peak of 15¾ percent. With the help of such developments, banks were able to maintain a favorable spread between their return on assets and their cost of funds. Money-center banks in particular benefited from the large expansion in business loans at rates tied to the higher prime rate. Regional banks meanwhile profited from portfolios heavily weighted with high-interest-rate mortgage and consumer loans, even though rates on such loans did not rise as fast as the business prime.

Nonetheless, the cost of bank funds rose steeply as the year progressed, especially in view of a shift from less costly sources of funds (those subject to deposit-rate ceilings) to more expensive sources acquired at accelerating market rates. Money-market certificates largely replaced less-expensive savings deposits, and their cost climbed as Treasury-bill rates rose. Even the "core" savings deposits became more expensive after midyear, with a rise in the Regulation Q ceiling rate from 5 to 5¼ percent. Costs on other liabilities—large CD's, Eurodollars, Federal funds and discount-window borrowings—all rose to record highs after October 6. Moreover, many banks after that date became subject to the 8-percent marginal reserve requirements on increases in "managed liabilities" such as CD's and Eurodollars. Offsetting these factors, income statements at many banks benefited from a reduction in loan-loss reserves, which reflected their improved experience with loan write-offs and write-downs. Overall, banks' profit experience in 1979 reflected an impressive ability to weather a highly volatile interest-rate environment.

WESTERN BUSINESS

The widely heralded recession failed to appear in the West during 1979, as most industries confounded the experts and posted substantial gains in sales and payrolls. (This region, which is served by the San Francisco Federal Reserve District, includes all nine states west of the Continental Divide—see map, page 23.) Some weak spots were evident—in the housing market, for instance—and these were aggravated by a severe inflation which sapped the strength of an otherwise healthy four-year-old expansion. Most analysts expect those weaknesses to lead to a slowdown in 1980, but the dip (if any) should be quite modest in comparison with the downturn anticipated elsewhere in the nation.

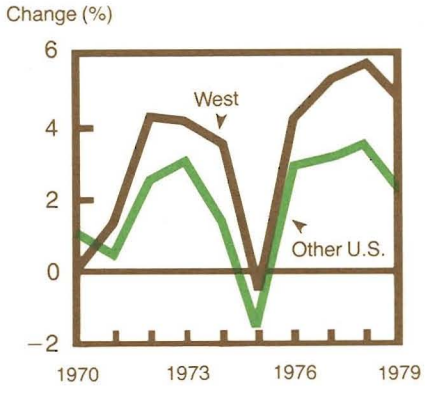
In 1979 as in other recent years, population growth provided a strong underpinning for economic growth. Since the 1970 census, in fact, the West's population has increased by roughly 5 million, bringing the regional total to about 35½ million. Migration accounted for roughly half of that total population gain, creating double-digit growth in almost every Western state. This means additional political as well as economic power, because the reapportionment following the 1980 census will probably mean one or more new House seats for California, Washington, Arizona, Oregon and Utah.

JOB GROWTH

During 1979, civilian employment in this nine-state area jumped almost 5 percent—an increase of roughly 800,000 new jobs—to reach a new peak of 16.0 million. The job expansion lagged only the unsustainable pace set during the 1977-78 boom. Also, in terms of jobs as well as population, the West continued to outpace the rest of the nation, as it has done since the early 1970's—indeed, in 1979, jobs increased twice as fast in the West as elsewhere. Employment gains were substantial almost across the board, especially in aerospace manufacturing and a wide range of service industries. The only exception was the government sector, where employment remained almost flat because of tight fiscal controls in practically every jurisdiction.

Reflecting the active job market, regional unemployment dropped from about 6.8 percent of the labor force in 1978 to roughly 6.2 percent in 1979. The improvement was evident in almost all Western states. California in particular

Change in Employment



brought its jobless rate into line with the national rate in late fall. For more than a decade, that state's jobless rate had hovered one or two percentage points above the national rate, because of heavy in-migration and problems with key regional industries. Indeed, at the beginning of the recovery in 1975, its jobless rate exceeded 10 percent, but after a four-year-long expansion less than 6 percent of the state's labor force was counted as unemployed.

Personal income in the West increased about 14½ percent in 1979, to about $345 billion—the largest annual gain of this expansion period. But most of the gain was eaten up by inflation, as consumer prices rose about 11½ percent between 1978 and 1979. Retail sales remained strong through much of the year—considerably stronger than elsewhere—reflecting the gains in real as well as nominal income. Moreover, new-car registrations ran substantially higher than a year ago, at least prior to the opening of the weak 1980 model year.

TAX REVOLT

For the second straight year, a widespread tax revolt dominated the political economy of the Western states, as voters continued to place tax- or spending-limitation measures on the books. In 1979, California voters passed the Proposition 4 ("Spirit of 13") initiative by a massive 3-1 margin—an even greater margin than they gave the Proposition 13 tax-reduction initiative the year before. The new measure prohibits California state and local governments

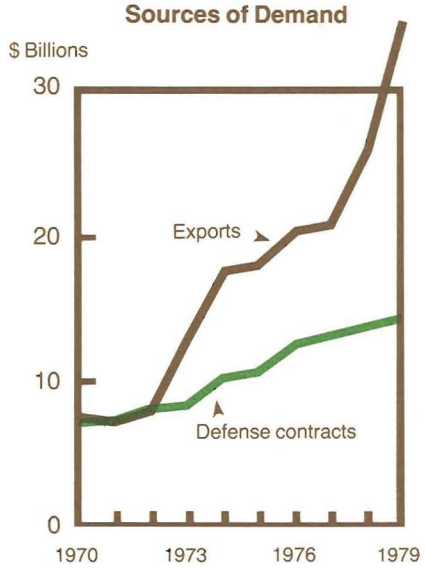
from increasing their spending any faster than increases in the consumer price index, plus proportional adjustments for population growth. In 1980, the California electorate will vote on a more drastic measure, popularly called "Jaws II," which would reduce state income-tax payments by half, and apply an indexing formula to all such payments in the future.

The latest initiatives reflect the dissatisfaction of Proposition 13's proponents with the legislative reaction to that measure. Prop 13 reduced California local property-tax revenues by 57 percent, but its effects were largely overcome by state "bail-out" transfers of $4.4 billion in 1978 and $4.8 billion in 1979. But in the process, the state government ran a deficit for two years in a row, depleting its once massive surplus—in effect, simply postponing the day of reckoning for local governments. On the other hand, Proposition 13's critics also found much to complain about; they argued, for example, that it reduced local autonomy by shifting tax and expenditure decisions to Sacramento, and that it raised debt-financing costs by making it impossible for local governments to issue new general-obligation debt.

MANUFACTURING GROWTH

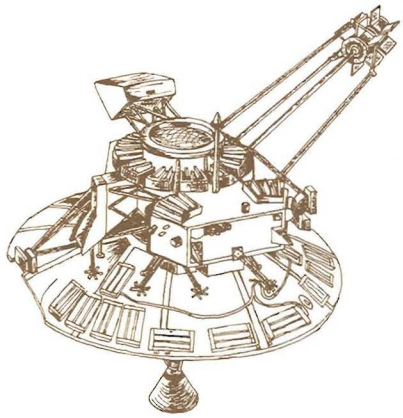
Regional income growth benefited in 1979 from a stronger-than-national expansion of manufacturing production, and also from a widening wage differential between the West and the rest of the nation. The key aerospace-equipment industry experienced boom conditions,

Sources of Demand



which spurred an 8-percent increase in industry employment over the course of the year. The main market stimulus came from the world airline industry. The airlines, responding to rapid passenger-traffic growth and to the imperative to improve fuel efficiency, continued to place large orders for both the present and next generation of jet transports. Defense and space business also increased as Western firms received more funding for production contracts, not to mention development contracts for new programs such as the MX mobile missile and the air-launch cruise missile. The electronic-equipment segment of the industry benefited from increased consumer purchases of its products, such as the electronic games which dominated Christmas toy counters.

The regional steel industry recorded only a 3-percent rise in production for the year, as buyers dipped into inventories to meet increased demand for heavy-construction steel and other products. The "trigger price" mechanism helped reduce imports sharply, by raising the minimum permissible price for foreign steel. Even this provided little support for the regional industry, however, and two major producers late in the year announced plans to close some of their higher-cost basic-steel and fabricating facilities. In contrast, the aluminum industry operated at virtually full capacity during 1979, as it strained to meet the increase in demand from aerospace and other industries. Its operations were somewhat hampered,



however, by dry weather in the Northwest, which forced a late-year cutback in power supplies from Federal hydro-electric facilities.

The copper industry benefited from increased worldwide consumption—plus heavy speculative demand, which reflected the use of copper (and not simply gold and silver) as an anti-inflation hedge. Accordingly, regional producers reactivated some of the mine and refinery capacity shut down during the inventory buildup of the preceding year. In the process, they posted a sharp 40-percent rise in the price of refined metal during 1979. Western silver miners, who produce about half of the nation's silver, meanwhile experienced a quadrupling of prices over the course of the year, and responded with a flurry of exploration and development at a number of historic mining locations.

PETROLEUM PROBLEMS

The supply problems and consequent upsurge in world oil prices that resulted from the Iranian revolution helped to limit the growth of the regional petroleum market. Western utilities and industrial plants boosted their demand for fuel oil, but gasoline consumption rose only slightly, reflecting last spring's sudden shortages and gas lines. Still, regional crude-oil production increased sharply for the third straight year, as the Alaskan pipeline's capacity (and flowthrough) rose from 1.2 to 1.5 million barrels per day. The import share of the regional market continued dropping to 23 percent—it was 48 percent at the 1976 peak—as Western refineries substituted more and more Alaskan oil for imports.

Much of the Alaskan oil was surplus to West Coast refinery needs, because of a mismatch between the product-mix demanded regionally and the product-mix available from high-sulphur Alaskan crude, and also because of the refineries' limited technical capability for processing that crude. Controversy surrounded alternative plans for transporting the surplus oil to Eastern U.S. markets, such as a proposed pipeline between Southern California and Texas, or between Puget Sound and Minnesota. With no progress on that front, the industry continued to rely on the inefficient method of shipping surplus oil by U.S.-flag tanker to the Gulf and East Coasts via the Panama Canal. But no one doubted that the nation could use every drop of oil that it could obtain from Alaskan and other domestic sources. Thus the oil industry paid a spectacular $2 billion for oil-and-gas development rights in the ice-choked Beaufort Sea off Alaska's northern coast, plus another $574 million for leases on Federal acreage off the Southern California coast.

CONSTRUCTION DEVELOPMENTS

The construction sector was dominated by a boom in nonresidential building, with contract awards rising almost 20 percent in 1979, or double the pace set elsewhere. Demand for industrial and commercial space was heavy in Southern California, and also in Seattle, Portland, Salt Lake City and other centers. The boom seems certain to continue in areas such as Seattle, which plans to build more office space in the next four years than it did in the last decade.

In contrast, the housing market represented the major weak spot in the regional picture during 1979, as housing starts dropped roughly 15 percent below the peak 1978 figure, to about 460,000 units. (That decline was roughly in line with the national decline.) Even so, inflationary cost pressures pushed the median price of new Western homes to $73,000 at midyear—18 percent above the mid-1978 level, and double the price of five years ago. Demand pressures remained high, reflecting the strong evidence that buying a home is one of the best hedges against inflation. But financing problems afflicted the industry during the year, because of the high costs and decreasing availability of mortgage money. With mortgage rates reaching as high as 14 percent in late 1979, many prospective buyers were priced out of the market, especially those living in communities subject to usury-law rate limits. But financial institutions continued to have some funds available—in contrast to their plight during earlier housing crunches—because of their ability to attract funds through new money-market certificates.

The national and regional housing decline reduced the flow of incoming orders at Western lumber mills, resulting in a 4-percent drop in production for the year. But a heavy backlog of unfilled 1978 orders, plus the rising cost of timber from public lands, pushed softwood-lumber prices to historic highs. In September, producer prices stood 14 percent above the year-earlier figure and more than double the average level reached during the 1974 recession. But with the acceleration of the housing slide, prices declined to about the year-earlier level by year-end. The pulp-and-paper segment of the industry meanwhile experienced sharp price increases throughout the year, because of strong demand, rising costs and a prolonged early-1979 strike at Pacific Northwest mills.

FARM EXPANSION

Despite substantial increases in production costs, the Western farm economy recorded a significant gain in net income on the basis of continued strength in domestic and foreign demand. Moderate overall temperatures and adequate water supplies generally provided excellent growing conditions, and farmers and ranchers produced bumper crops of many commodities. The decline of cattle herds meanwhile slowed after nearly four years of liquidation, in response to high beef prices and improved grazing conditions. Export markets for Western products remained very strong as a result of the continued weakness of the dollar and the continued upsurge of world food demand.

Farm cash receipts increased almost 25 percent for the year, with healthy gains in both the crop and livestock sectors. Crop receipts generally benefited from strong production gains, which offset weakening prices in some sectors. The citrus crop, for example, was 19 percent larger than the frost-affected 1978 crop, and the California cotton crop was 16 percent larger than the 1977 record. Crops of rice, nuts, feed grains and most fresh vegetables also posted significant gains. One notable exception, however, was potatoes, as Idaho produced its smallest crop of the past four years. Wheat production failed to match the bumper 1978 crop, and prices ran about 20 percent higher than a year ago.

Cattlemen appeared to be moving out of the trough of the cattle cycle, as California and Oregon ranchers began to rebuild their herds, offsetting most of the decline recorded elsewhere in the West. But along with herd rebuilding went a cutback in beef production, which boosted beef prices by nearly 22 percent and stimulated production of hogs and poultry. Record broiler production, for example, occurred both in regional and national markets, leading to some softening in the price of this product. Ranchers benefited from improved range and grazing conditions, which helped them offset a sharp 16-percent increase in feed costs.

Agricultural exports increased 11 percent to $458 million, partly on the basis of heavy Asian and Eastern European demand. Shipments of hides, feed grains and vegetables were especially strong. Global demand for wheat kept wheat prices high, despite an increase in production of 14 percent worldwide.

RECESSION IN 1980?

On balance, 1979 turned out to be a rather solid year for the Western economy, but 1980 could be somewhat more somber. The housing industry seems likely to decline even further, given the high price of housing and the decreased availability of mortgage money. (This means problems too for the Northwest's lumber industry.) Debt- and inflation-ridden consumers seem likely to reduce their purchases of postponable big-ticket items, primarily autos, given their need to budget first for increasingly expensive necessities. Most importantly, a worsening energy situation could spell trouble for the West's tourist industry and many other industries besides.

Yet withal, the West seems certain to get through 1980 with less damage than the national economy, perhaps with only a modest dip in its growth rate. The structure of the regional economy is in its favor, since it exhibits a smaller concentration of cyclical industries such as autos, and a greater concentration of relatively recession-proof industries such as trade and services. Another plus is the likelihood of a continued boom in the key aerospace-manufacturing industry. That industry holds a bulging orderbook full of new business from the world's airlines and also from the Pentagon, which is boosting its spending in real terms for the first time in a decade. The strength of overseas demand for the region's farm products and high-technology products, especially in the fast-growing Pacific Basin countries, also should provide underpinning for the Western economy. The overall outlook, then, is for a slowdown but not a major recession during 1980.

WESTERN BANKING

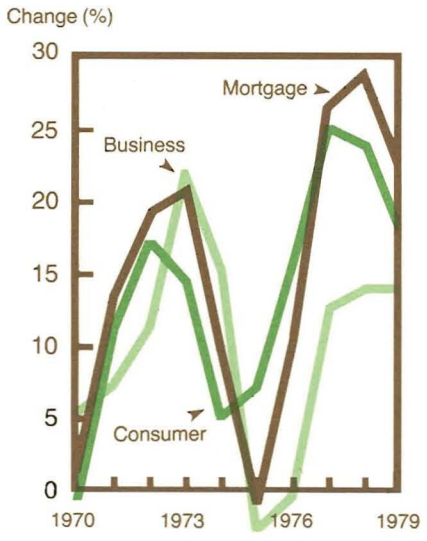
Banking activity, like business activity, expanded more rapidly in the West than elsewhere during 1979. Total loans and investments at District banks' domestic offices reached $170 billion by year-end, for a 14-percent overall increase. Loan portfolios (up 16 percent) grew by several percentage points more than they did at banks elsewhere, while securities portfolios (up 5 percent) rose at a lower rate. Real-estate and consumer loan demand continued almost unabated throughout the year, and business loans showed considerable strength for three quarters before tailing-off in late 1979. And unlike their 1978 experience, Western banks managed to increase their securities portfolios in the face of strong loan demand, expanding their holdings of agency and municipal debt to provide a liquidity cushion as well as collateral for public deposits and other such liabilities.

STRONG LOAN EXPANSION

Business loans increased 14 percent during the year, and the pace was even stronger before the Federal Reserve's credit-tightening moves of October 6. But thereafter, borrowers became more cautious when faced with a 15¾-percent prime rate, and lenders became more cautious because of the extra costs of funding loan growth under the new marginal reserve requirement on "managed liabilities." Most industry groups substantially expanded their borrowings at Western banks during the year. By size, the heaviest borrowers were "middle market" firms—those small and medium-sized firms which must rely primarily on bank financing for expansion and working capital. Western banks, unlike Eastern banks, experienced little increase in borrowing by large corporations; many such firms apparently continued to rely heavily on the commercial-paper market, where funds were available at lower cost.

Despite the downturn in new housing activity, real-estate financing remained very strong—at least at banks if not other financial institutions—until record mortgage rates and housing prices began to take their toll in late 1979. The 23-percent gain in District banks' mortgage portfolios was exceeded only by the massive 29-percent gain of the previous year. The heaviest financing activity occurred in connection with the construction of conventional single-family housing, but farm real-estate lending also grew rapidly. At year-end, outstanding mortgage loans exceeded $52 billion, at which point they constituted 37 percent of total loan portfolios.

Western Bank Loans



Undaunted by record levels of personal debt, households continued to draw heavily on their bank credit lines and to use bank financing for autos, mobile homes, and other big-ticket items. The borrowing pace began to slacken in the final quarter, however, as new credit extensions slowed in line with a weakening of auto sales and a more cautious mood on the part of buyers and lenders.

NEW DEPOSIT SOURCE

Western banks financed their growing loan volume by obtaining about $10 billion in new deposits, about $9 billion of which were in six-month money-market certificates (MMC's). With their rates tied to the Treasury bill rate, these certificates have helped counter disintermediation—the outflow of funds into money-market instruments—ever since their appearance in mid-1978. However, they have also attracted considerable amounts of funds from banks' own deposits, leading to an actual decline in the savings-deposit category;

as a result, MMC's now account for about one-fifth of District banks' consumer-type time and savings deposits. In the second half of the year, banks also relied heavily on large negotiable certificates (CD's) to raise funds, as a means of meeting the strong loan demand and renewed savings-deposit outflows.

Moreover, Western banks acquired several billion dollars more from a broad range of nondeposit sources of funds. (These sources include Federal funds, securities repurchase agreements, Eurodollars, and loans sold outright to bank holding companies.) For example, large District banks' net purchases (borrowings) in the Fed-funds market averaged over $800 million—up slightly from 1978, but well below the 1974 peak. Until the Federal Reserve's October 6 action, these "managed liabilities" were not subject to reserve requirements. Even after that date, however, most banks remained under their reserve-free limit, and thus were able to avoid the additional reserve requirement.

Federal Reserve member banks in the West meanwhile took more advantage of their borrowing privilege at the Federal Reserve Bank of San Francisco. Discount-window borrowing reached $120 million on a daily average basis—more than double the 1978 figure, although considerably less than in the 1973-74 tight-money period. This sharp increase reflected the effects of an increasingly restrictive monetary policy, as well as the widening rate spread between two alternative sources of funds, the Fed-funds market and the Federal Reserve's discount window.

HIGHER EARNINGS

Western banks' earnings rose to record levels in 1979, according to preliminary estimates. Operating income rose substantially because of heavy loan volume, plus record interest rates on commercial and real-estate lending, as was true of banks elsewhere in the nation. But Western banks also benefited from their heavy retail orientation, with a large proportion of high-yielding consumer and mortgage loans in their portfolios, even though rates on such loans did not rise as fast as the prime.

Offsetting these income gains somewhat were dramatic increases in bank costs, especially the cost of new funds. Rates on large CD's, Eurodollars, Federal funds, repurchase agreements and money-market certificates all reached record levels during 1979. Within the deposit category, interest expense also rose as individuals shifted their funds out of passbook savings and fixed-rate time certificates into the more costly variable-rate MMC's. Moreover, Western banks in particular, with their heavy concentration of savings deposits, keenly felt the impact when regulatory authorities raised the ceiling rate on such deposits by ¼ percentage point in July. However, the cost of these consumer deposits was still well below the cost of large CD's.

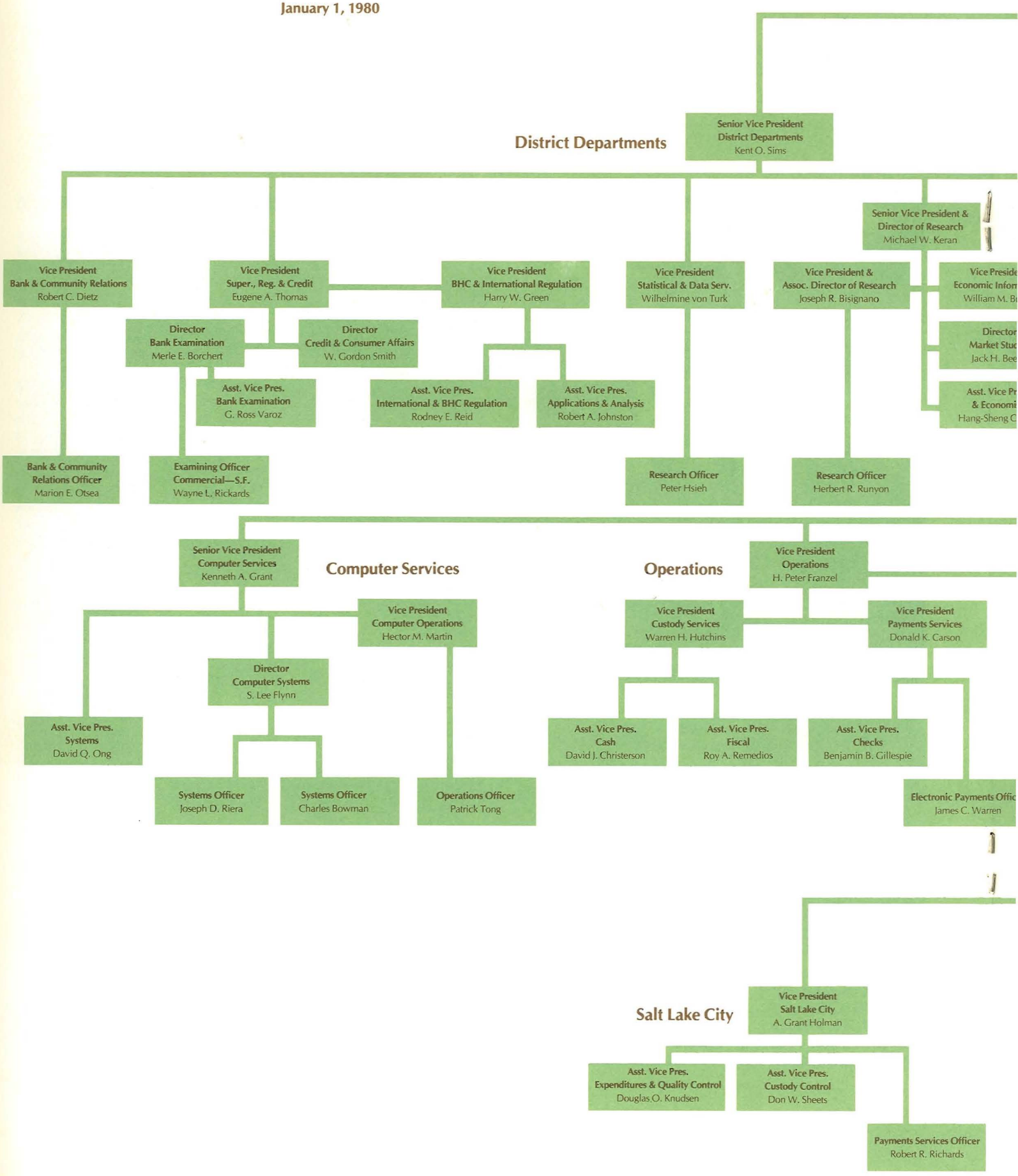
UNCERTAIN OUTLOOK

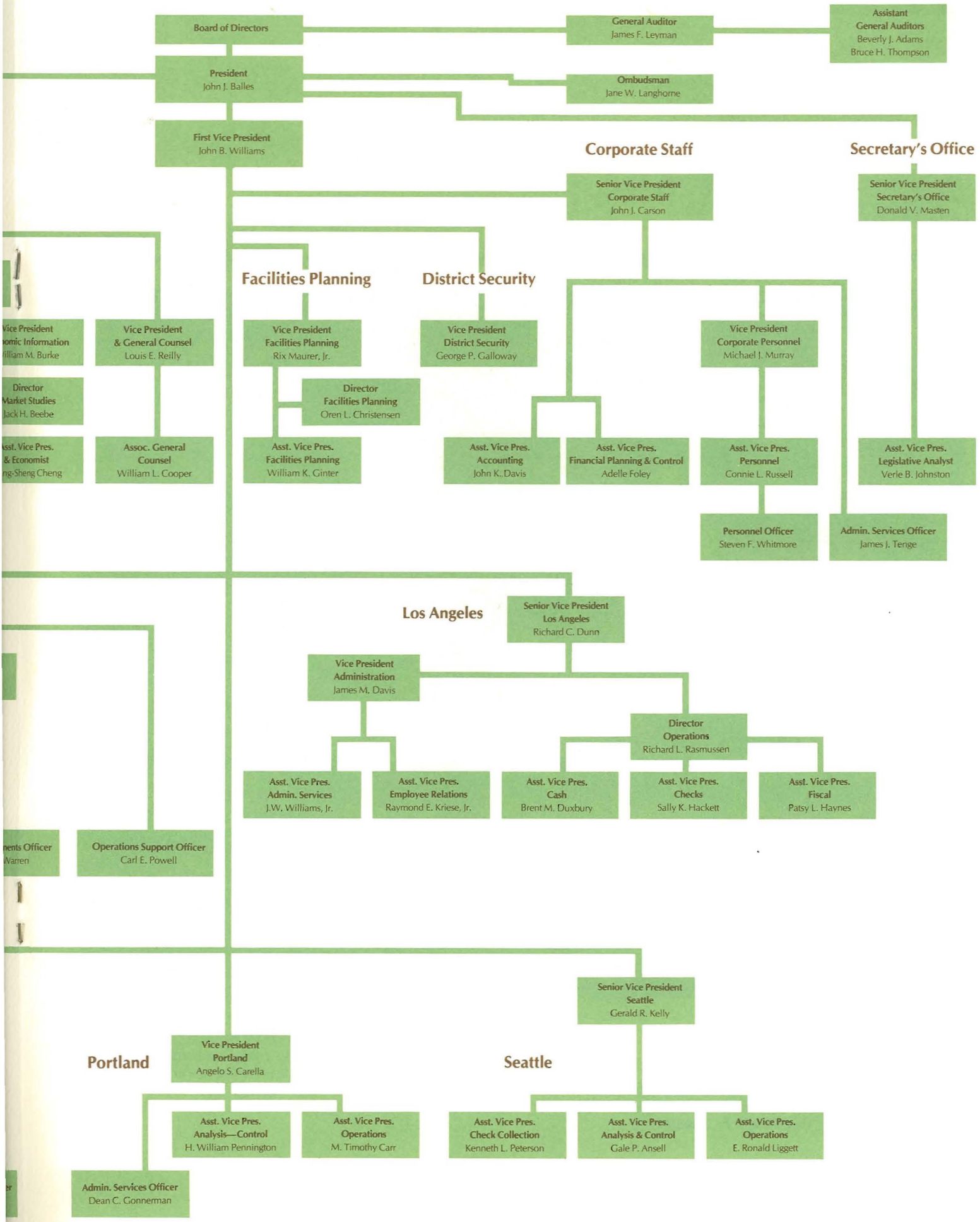
A slowdown in the regional economy would spell a more uncertain climate for Western commercial banking in 1980. Banks should experience a deceleration from last year's strong lending pace, although lending to the business sector may increase in the event of a slowdown-caused decline in corporate liquidity. Loan demand from the household sector should weaken, as a reflection of a more sluggish buying pace for housing and consumer durables. In 1980, as in earlier periods of reduced business activity, consumers may be expected to put more emphasis on reducing debt and building up savings. On the liability side, meanwhile, Western banks will probably continue using money-market certificates as a major source of funds.

Revenues may decline somewhat because of both a reduction in loan growth and a drop in the return on those loans, yet for Western banks at least, that decline should be cushioned by their disproportionately large holdings of high-yielding mortgage and consumer loans. On the other hand, banks' interest expense also would be reduced if money-market rates decline. In this situation, banks may be able to maintain or even improve the spread between their return on assets and their cost of funds—although any increase in margins could be partly offset by an expected increase in loan losses and loan delinquencies. But in the last analysis, Western banks' earnings should expand faster than the earnings of their national counterparts, simply because of the likelihood of a stronger business environment in the West than elsewhere.

Management Committee
(Shown from left to right)
Kent O. Sims, Senior Vice President, District Departments
John J. Balles, President
John B. Williams, First Vice President
John J. Carson, Senior Vice President, Corporate Staff

Federal Reserve Bank of San Francisco
Organization Chart
January 1, 1980




Board of Directors
General Auditor
James F. Leyman
Assistant General Auditors
Beverly J. Adams
Bruce H. Thompson
President
John J. Balles
Ombudsman
Jane W. Langhorne
First Vice President
John B. Williams
Corporate Staff
Secretary's Office
Senior Vice President
Corporate Staff
John J. Carson
Senior Vice President
Secretary's Office
Donald V. Masten
Facilities Planning
District Security
Vice President
& General Counsel
Louis E. Reilly
Vice President
Facilities Planning
Rix Maurer, Jr.
Vice President
District Security
George P. Galloway
Vice President
Corporate Personnel
Michael J. Murray
Director
Facilities Planning
Oren L. Christensen
Assoc. General
Counsel
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Facilities Planning
William K. Ginter
Asst. Vice Pres.
Accounting
John K. Davis
Asst. Vice Pres.
Financial Planning & Control
Adelle Foley
Asst. Vice Pres.
Personnel
Connie L. Russell
Asst. Vice Pres.
Legislative Analyst
Verle B. Johnston
Personnel Officer
Steven F. Whitmore
Admin. Services Officer
James J. Tenge
Los Angeles
Senior Vice President
Los Angeles
Richard C. Dunn
Vice President
Administration
James M. Davis
Director
Operations
Richard L. Rasmussen
Asst. Vice Pres.
Admin. Services
J.W. Williams, Jr.
Asst. Vice Pres.
Employee Relations
Raymond E. Kriese, Jr.
Asst. Vice Pres.
Cash
Brent M. Duxbury
Asst. Vice Pres.
Checks
Sally K. Hackett
Asst. Vice Pres.
Fiscal
Patsy L. Haynes
Operations Support Officer
Carl E. Powell
Senior Vice President
Seattle
Gerald R. Kelly
Portland
Vice President
Portland
Angelo S. Carella
Seattle
Asst. Vice Pres.
Analysis—Control
H. William Pennington
Asst. Vice Pres.
Operations
M. Timothy Carr
Asst. Vice Pres.
Check Collection
Kenneth L. Peterson
Asst. Vice Pres.
Analysis & Control
Gale P. Ansell
Asst. Vice Pres.
Operations
E. Ronald Liggett
Admin. Services Officer
Dean C. Gonnerman

Branch Operations
(Shown from left to right)
A. Grant Holman, Vice President, Salt Lake City
Angelo S. Carella, Vice President, Portland
H. Peter Franzel, Vice President, Operations Support
Richard C. Dunn, Senior Vice President, Los Angeles
Gerald R. Kelly, Senior Vice President, Seattle

WESTERN CENTRAL BANK

During 1979, the Federal Reserve Bank of San Francisco provided expanded central-bank services—in the areas of checks, coin, currency, fiscal agency, and electronic funds transfers—for a regional economy which continued to grow at a faster pace than the rest of the nation. The Twelfth District, which contains five Reserve Bank offices (San Francisco, Los Angeles, Portland, Salt Lake City and Seattle) is the largest Federal Reserve District in terms of both population and geographic size. It includes the states of Alaska, Arizona, California, Hawaii, Idaho, Nevada, Oregon, Utah and Washington, plus the territories of Guam and American Samoa, and it serves 35½ million people and 625 banks with a total of 7,114 banking offices.

The Reserve Bank's scope of operations in 1979 reflected the large size of its service area. For example, Bank staff handled about 1.5 billion paper checks, not to mention 1.9 billion coins and 1.4 billion pieces of currency. At the same time, the Bank continued to extend its electronic-payments capability, through such means as automated clearing-houses, Government direct-deposit programs, and the Federal Reserve wire-transfer network. District member banks transferred $8.9 trillion throughout the country over the Fed Wire network. The staff continued to work on a five-year automation program, with an eye toward further internal efficiencies as well as improved services for commercial banks and the general public.

MEMBERSHIP DEVELOPMENTS

Declining membership became a problem for the San Francisco Reserve Bank, as it had been earlier for the Federal Reserve System generally. In this District, the number of member banks remained almost stable, as 7 state-chartered banks became members while10 banks went off the membership rolls. However, deposits held by banks withdrawing from membership exceeded the deposits gained from new members, primarily because most of the latter group were small, newly organized institutions. The System nation-wide experienced a net loss of more than 75 member banks during the year. As these numbers suggest, it has become increasingly difficult to maintain membership in a situation where member banks (unlike nonmember institutions) cannot earn a return on their required reserves.

Both the House and the Senate held lengthy hearings on this subject during the year, but failed to act on final legislation before year-end. The bills under consideration generally would reduce the number of institutions subject to reserve requirements, but would extend the principle of coverage to all those that handle check-like transactions accounts. Proposed legislation also would provide wider access to discount-window borrowing and other Federal Reserve services, but in addition would impose charges for Fed services.

During the year, the Reserve Bank's bank-relations personnel organized meetings for bankers throughout the District, to explain the reasons for the System's legislative proposals and the need for a strong and independent central-banking system. In addition, they worked to solve bankers' problems by providing technical advisory services for member banks, cost-of-membership studies for potential members, and a series of seminars on economic and financial developments for banking and business audiences. The Reserve Bank continued to offer member banks a functional-cost analysis program, which takes advantage of the Federal Reserve's unique ability to construct regional and national peer-group comparisons from accounting data supplied by its members. To supplement the basic System program, which is designed primarily for small and medium-sized institutions, the San Francisco Bank developed a special program for the large banks which characterize this District.

SUPERVISORY RESPONSIBILITIES

In the area of supervision and regulation, the Reserve Bank began taking on new responsibilities conferred by the International Banking Act of 1978, which extended Federal control over the branches and agencies of foreign banks operating in this country. Reserve Bank personnel cooperated with other Federal bank-supervisory agencies and various state agencies with compliance responsibilities under the Act—for example, by helping to develop a uniform examination report for nation-wide use, and by working with the California State Banking Department on plans for a joint examination of California agencies of foreign banks in 1980. Bank personnel also became heavily involved in the Federal Reserve's first significant revisions in 15 years of its Regulation K (International Banking Operations). Again, the Bank participated in the important work of the Inter-Agency Country Exposure Risk Committee, which evaluates on a uniform basis the relative risk of extending credit to public and/or private entities in some 75 countries throughout the world.

During 1979, the Reserve Bank received 142 bank holding-company applications for analysis and processing, along with 58 other applications involving structure changes as well as 33 applications for foreign activities. The applications staff maintained close communication with active holding companies and other applicants, and provided interpretations and advice to those wishing to expand or restructure their operations.

In 1979, the Federal Reserve System as a whole began its first year of operation with a standardized inspection report and uniform rating system, somewhat along the lines of the inspection program developed earlier by the San Francisco Reserve Bank. This Bank adopted a policy in 1976 of scheduling the inspection of major holding companies concurrently with the examination of their principal subsidiary bank by this or other regulatory agencies. The policy achieves some efficiencies by pooling knowledge among all of the bank regulatory agencies involved in the supervision of each holding-company family, while even greater savings are realized by the holding companies and banks being examined. The Fed's Board of Governors has formally adopted this policy for implementation System-wide during 1980.

CREDIT, CONSUMER ACTIVITIES

Following a recent System policy change, the Bank established guidelines and implemented procedures permitting member banks to pledge residential mortgage loans and municipal obligations at the discount window, yet retain physical possession of paper representing this collateral. The Bank, a long-time advocate of such "off-premises custody" arrangements, was among the first in the System to institute these procedures. In a related action, the System formally provided for the acceptance of foreign paper as discount-window collateral, in line with procedures adopted at this Reserve Bank several years ago. San Francisco held more than three-fourths of the foreign collateral pledged at all Reserve Banks during 1979. These policy changes helped expand the pool of collateral available for discount-window borrowings, and reduced the administrative burden associated with banks' pledging of collateral.

The consumer-affairs staff conducted examinations at all state-member banks, and also at about one-third of their branches, in line with an expanded System-wide program designed to achieve broad-based compliance with consumer-protection laws and regulations. In addition, the staff conducted formal advisory programs for member banks, as part of a service in which specially trained examiners provide on-site educational and advisory work. The Reserve Bank received 604 individual consumer complaints against commercial banks, and of that total, processed 138 complaints which were related to institutions for which the Bank is the primary supervisor. Also, the staff received several thousand requests for information from the general public, many of them in response to a series of Bank-produced public-service announcements on consumer regulations, which were shown on a number of television stations in the District.

COMPUTER DEVELOPMENTS

The Bank continued to implement a long-range automation plan, which calls for District-wide standardization and centralized processing of most operations, with all five District offices tied together via a modern computer network operated out of the San Francisco data center. All offices now have centralized services available in certain areas, such as tax-receipt processing and some savings-bond processing. Major automation projects completed in 1979 included a District-wide central-adjustments system to handle account reconciliations with member banks, a high-speed telecommunications system which provides better message-switching services between member banks, monitoring programs to help manage check-processing float, and a new system to handle the increased reporting burden associated with banks' foreign-exchange operations.

In a major ongoing project, the Bank continued development work on a sophisticated system to handle the processing of financial reports received from banks and other financial institutions. The increasing number of reports and respondents, in addition to the increasing visibility and sensitivity of the monetary aggregates which are drawn from these data, make completion of this project our highest priority effort.

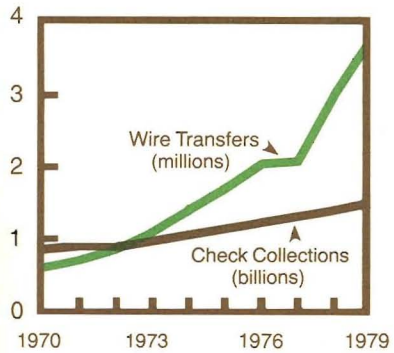
Data processing and fiscal personnel continued work on the automation of a Treasury-securities inventory and transfer system (called SHARE). San Francisco is the lead district on this project, which will provide a standardized on-line database fiscal-computer application servicing 13 offices in the Kansas City, St. Louis and San Francisco districts. This is the first large-scale joint automation project undertaken within the Federal Reserve System.

PAYMENTS SERVICES

In the check-processing activity, Bank staff handled 1.3 billion paper checks during the year—a substantial 6-percent increase. With continued technological and operational improvements, check personnel maintained the highest check-processing productivity in the Federal Reserve System. At the same time, the quality of operations was significantly improved. As a result, internally generated errors which require costly and time-consuming adjustment were reduced by more than 35 percent.

In 1979, as in earlier years, the fastest-growing means of payment was electronic. While check-processing activity increased 6 percent, wire funds transfers increased 23 percent, and automated clearinghouse (ACH) and government deposit activity jumped 44 percent. In dollar terms, District member banks settled a massive $8.9 trillion through the Federal Reserve's wire-transfer system during the year. But the sharpest percentage gain occurred at automated clearinghouses, which move funds by electronically-transmitted payment instructions that take the place of paper checks. The Bank expanded ACH operations to a 24-hour per day processing schedule in October, as part of a System effort to attract additional volumes by setting schedules more accommodating to corporate originators.

Checks and Wire Transfers



In cooperation with the Treasury Department, the Bank completed implementation of a government-check truncation program which had been instituted in 1978. Truncation involves shipping magnetic tapes and microfilm copies of checks, instead of the original paper checks in bulk, to the Treasury computer-operations center, enhancing speed and control. This effort was a major accomplishment, as the San Francisco District processes the largest volume of government checks in the System—124 million in 1979.

CASH AND FISCAL ACTIVITIES

Despite the increase in check usage and the rapidly accelerating growth in electronic payments, the Reserve Bank continued to handle substantial amounts of coin and currency in 1979. Altogether, it received and counted 1.9 billion coins and processed 1.4 billion pieces of currency during the year. Currency verification decreased by 45 percent, reflecting several major efficiencies which were adopted in 1978. For example, commercial banks now deposit excess fit currency in sealed plastic bags, so that the currency can then be paid out to the same bank without the need for Reserve Bank verification and counting. In another major advance, the Bank installed three high-speed currency machines in 1979, and will install three more in 1980. Each machine has an optimum feed rate of 1,200 notes a minute, and is capable both of detecting counterfeits and of destroying, on line, those notes which do not meet fitness standards. Over time, the new equipment will help reduce staff in this labor-intensive activity, and will also improve processing efficiency.

In the coin area, the major activity centered around the release of the Susan B. Anthony dollar coin, which was made available to the public on July 2, 1979. This Bank distributed about 65 million coins to District financial institutions, representing one-fourth of the total volume distributed nationwide. Demand for the coin fell off considerably after the initial release. However, the Treasury and Federal Reserve System have continued to promote the coin, maintaining that overall savings of $50 million a year could be realized by replacing the present pool of dollar bills with Anthony dollar coins.

In its role as fiscal agent for the U.S. Government, the Reserve Bank handled substantial amounts of public-debt instruments in the form of savings bonds, marketable Treasury securities and food stamps. Activity in marketable securities increased 25 percent in volume, reflecting investor attraction to the double-digit interest rates offered on such issues. At the same time, the Bank worked to improve computer handling of securities through such means as the aforementioned joint automation project with the Kansas City and St. Louis Districts.

The Bank completed implementation of the Treasury-designed tax-and-loan investment program. Under this arrangement, the Treasury earns interest by investing its operating cash balances while paying fees for certain services which it formerly received free from financial institutions. Other changes in fiscal processing included revisions to the savings-bond program. First, the Treasury accelerated payments for savings bonds

sold by financial institutions acting as issuing agents. Second, it announced two new series of savings bonds, EE and HH, to replace the current E and H bonds.

IMPROVED PRODUCTIVITY

The San Francisco Reserve Bank operated at the second highest level of cost effectiveness in the System, with an aggregate unit cost 9 percent below the System average. Productivity (output per worker-hour) in these operational activities has increased 65 percent in the past five years. The Bank achieved this performance while experiencing only slight increases over 1974 unit-cost levels, despite sharply rising costs of salaries, materials and equipment.

Lastly, and of most far-reaching consequence to the Bank's operations, work has begun on a new 12-story, 653,000-square foot building on San Francisco's Market Street. Ground-breaking is scheduled for early 1980 and the building should be ready for occupancy in 1982. The Bank's future productivity would be hampered if it were to continue operating at its present headquarters building, which was built in the 1920's and is small and inefficient from the standpoint of 1980-style banking operations. In addition to modern operations facilities, the new building will house a major economic-education exhibition treating principles of economics, the growth of the Western financial community, and the Federal Reserve's role in the regional and national economies.

SUMMARY OF OPERATIONS

	Dollar Value (Millions)		Volume (Thousands)	
	1978	1979	1978	1979
Custody Services				
Cash Services				
Currency paid into circulation	N/A	N/A	1,281,416	1,408,121
Coin	264	274	1,818,775	1,889,231
Fiscal Agency Services				
Savings Bonds	1,909	1,709	25,224	35,163
Other Treasury issues	1,007,721	1,006,206	340	424
Currency verified and destroyed	2,176	2,264	343,990	345,188
Food coupons	1,006	792	263,684	223,232
Payments Mechanism				
Check Processing				
Commercial checks	569,335	725,195	1,283,807	1,358,985
Government checks**	71,389	88,190	133,593	124,570
Return items	6,835	9,712	17,956	20,223
Electronic Funds Transfer				
Wire transfers	7,871,414	8,930,438	3,123	3,847
Automated clearinghouse	1,674	2,562	3,171	7,130
Government deposits	7,185	9,960	20,341	26,790
Discounts and Advances				
Total discounts and advances	12,073	28,952	914*	1,318*
Number banks accommodated	N/A	N/A	60*	59*
Noncash Collections	3,698	2,760	213	176

* Actual figures
** Including postal money orders

Twelfth Federal Reserve District

DIRECTORS

The Federal Reserve carries out its central-banking functions through a nationwide network of 12 Federal Reserve Banks and their 25 branches, under the policy guidance, coordination and general supervision of the Board of Governors in Washington, D.C. The Head Office of the Federal Reserve Bank of San Francisco has a nine-member Board of Directors. Each of the Bank's other offices at Los Angeles, Portland, Salt Lake City and Seattle has a seven-member board.

Federal Reserve directors bring management expertise to the task of overseeing Reserve Bank operations. They also provide first-hand information on key economic developments in various areas of the District, complementing the Bank's internal research efforts. In addition, Board members give advice on the general direction of monetary policy, especially with regard to the Bank's discount rate. The Head Office Board has specific responsibility for initiating changes in the discount rate, subject to review and approval by the Board of Governors.

SAN FRANCISCO

Chairman of the Board and Federal Reserve Agent

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Chairman, President and Chief Executive Officer
Kaiser Aluminum & Chemical Corp.
Oakland, California

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Caroline Leonetti Ltd.
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Alan C. Furth
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Southern Pacific Company
San Francisco, California

Frederick G. Larkin, Jr.
Chairman of the Executive Committee
Security Pacific National Bank
Los Angeles, California

Ole R. Mettler
President and Chairman of the Board
Farmers & Merchants Bank of Central California
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Robert A. Young
Chairman of the Board and President
Northwest National Bank
Vancouver, Washington

Federal Advisory Council
Chauncey E. Schmidt
Chairman, President and Chief Executive Officer
The Bank of California, N.A.
San Francisco, California

Maier

Ahmanson

Furth

Larkin

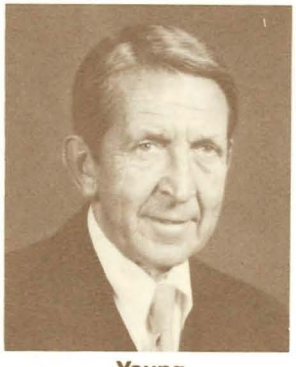
Mettler

Peck

Stamper

Federal Advisory Council

Vaughan



Young

Schmidt

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Harvey A. Proctor
Chairman of the Board
Southern California Gas Company
Los Angeles, California

Fred Andrew
President
Superior Farming Company
Bakersfield, California

James D. McMahon
President
Santa Clarita National Bank
Newhall, California

Bram Goldsmith
Chairman of the Board
City National Bank
Beverly Hills, California

Harvey J. Mitchell
President
First National Bank of
San Diego County
Escondido, California

Lola McAlpin-Grant
Assistant Dean
Loyola Law School
Los Angeles, California

Togo W. Tanaka
President
Gramercy Enterprises
Los Angeles, California

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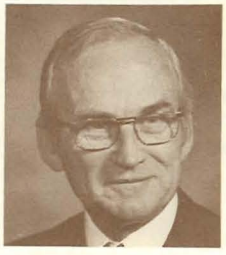
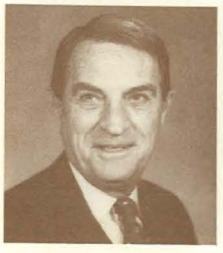
Chairman of the Board
Loran L. Stewart
Director
Bohemia, Inc.
Eugene, Oregon



Merle G. Bryan
President
Forest Grove National Bank
Forest Grove, Oregon



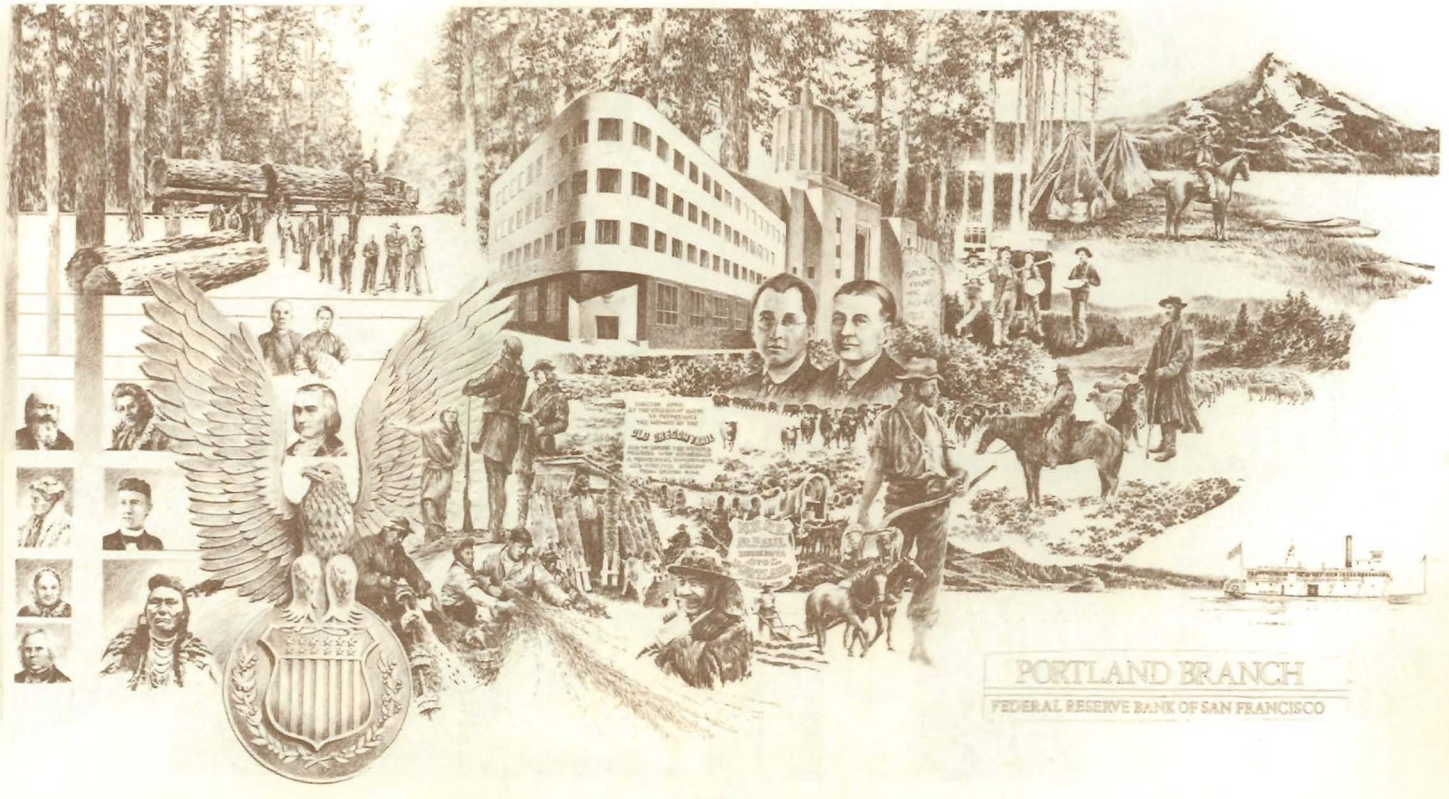
Phillip W. Schneider
Northwest Regional Executive
National Wildlife Federation
Portland, Oregon

Jack W. Gustavel
President and Chief Executive Officer
The First National Bank
of North Idaho
Coeur d'Alene, Idaho

Kenneth Smith
General Manager
The Confederated Tribes of
Warm Springs
Warm Springs, Oregon

Jean Mater
Vice President
Mater Engineering Ltd.
Corvallis, Oregon

Robert F. Wallace
Chairman of the Board
First National Bank of Oregon
Portland, Oregon



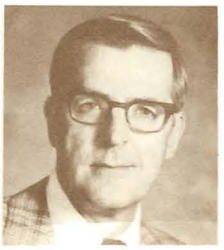
SALT LAKE CITY

Chairman of the Board
Wendell J. Ashton
Publisher
Deseret News Publishing Company
Salt Lake City, Utah

Robert E. Bryans
Chairman of the Board
Walker Bank & Trust Company
Salt Lake City, Utah

Mary S. Knox
Chairman of the Board
Idaho State Bank
Glenns Ferry, Idaho

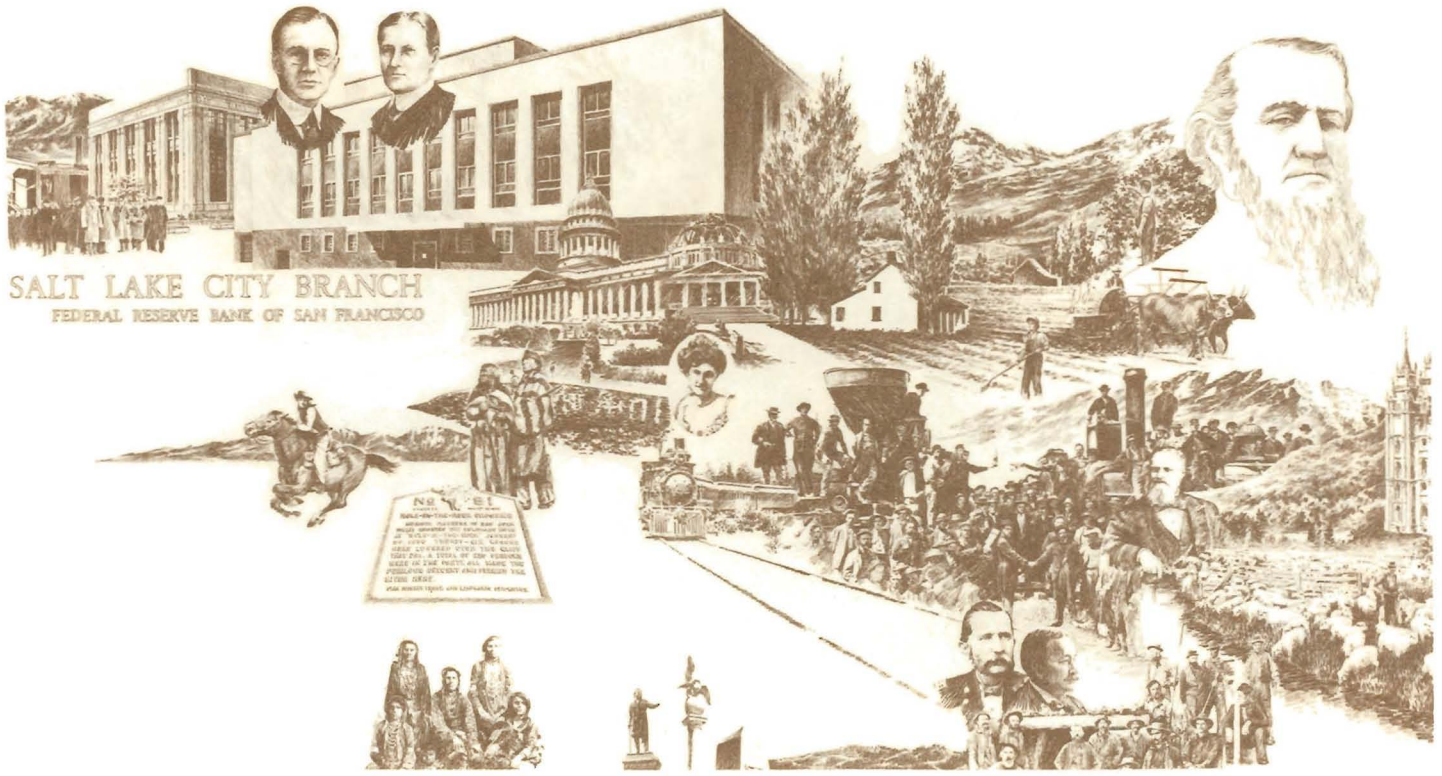
Robert A. Erkins
Geothermal Agri/Aquaculturist
White Arrow Ranch
Bliss, Idaho



Fred H. Stringham
President
Valley Bank and Trust Company
South Salt Lake City, Utah

David P. Gardner
President
University of Utah
Salt Lake City, Utah

J. L. Terteling
President
The Terteling Company, Inc.
Boise, Idaho



SEATTLE

Chairman of the Board
Lloyd E. Cooney
President and General Manager
KIRO-Radio & Television
Seattle, Washington

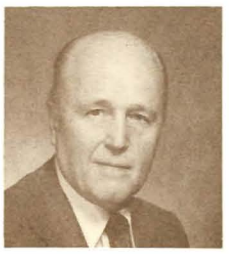
Merle Adlum
President
Puget Sound District Council,
Maritime Trades Dept. AFL-CIO
Seattle, Washington

Donald L. Mellish
Chairman of the Board
National Bank of Alaska
Anchorage, Alaska

C. M. Berry
President
Seafirst Corporation and
Seattle-First National Bank
Seattle, Washington

Virginia L. Parks
Vice President for Finance
and Treasurer
Seattle University
Seattle, Washington

Douglas S. Gamble
President and Chief
Executive Officer
Pacific Gamble Robinson Company
Seattle, Washington



Rufus C. Smith
Chairman of the Board
The First National Bank
of Enumclaw
Enumclaw, Washington

COMPARATIVE STATEMENT

(Thousands of Dollars)

	December 31, 1978	December 31, 1979
Assets		
Gold certificate account	1,299,982	670,016
Special Drawing Rights certificate account	152,000	211,000
Federal Reserve notes of other Federal Reserve Banks	−0−	−0−
Other cash	31,312	60,642
Loans to Member Banks:		
Secured by United States Government & Agency obligations	214,500	36,500
Other eligible paper	38,100	−0−
Other paper	−0−	84,100
Federal Agency obligations	1,046,745	1,080,827
United States Government securities:		
Bills	5,589,142	5,952,159
Notes	7,272,340	7,432,314
Bonds	1,652,506	1,914,520
Total United States Government securities	14,513,988	15,298,993
Total loans and securities	15,813,333	16,500,420
Cash items in process of collection	2,031,377	3,778,141
Bank premises	9,698	11,105
Operating equipment	8,555	10,497
Other assets:		
Denominated in foreign currencies	224,700	349,962
All other	1,507,133	459,492
Total assets	21,078,090	22,051,275
Liabilities		
Federal Reserve notes	12,132,792	13,193,695
Deposits:		
Total Member bank—reserve accounts	7,102,592	7,290,498
United States Treasurer—general account	594,391	337,362
Foreign	28,378	42,159
Other deposits	64,451	121,199
Total deposits	7,789,812	7,791,218
Deferred availability cash items	559,035	193,520
Other liabilities	291,977	508,166
Total liabilities	20,773,616	21,686,599
Capital accounts		
Capital paid in	152,237	182,338
Surplus	152,237	182,338
Total liabilities and capital accounts	21,078,090	22,051,275
Contingent liability on acceptances purchased for foreign correspondents	−0−	−0−

EARNINGS AND EXPENSES

(Thousands of Dollars)

	December 31, 1978	December 31, 1979
Current earnings		
Discounts and advances	3,895	12,644
United States Government securities	1,091,753	1,323,391
Foreign currencies	270	9,684
All other	53	43
Total current earnings	1,095,971	1,345,762
Current expenses		
Total current expenses	66,460	71,031
Less reimbursement for certain fiscal agency and other expenses	6,044	6,582
Net expenses	60,416	64,449
Profit and loss		
Current net earnings	1,035,555	1,281,313
Additions to current earnings:		
Profit on sales of United States Government securities (net)	−0−	−0−
Profits on foreign exchange transactions	−0−	−0−
All other	685	1,081
Total additions	685	1,081
Deductions from current net earnings:		
Loss on foreign exchange transactions (net)	70,795	515
Loss on sales of United States Government securities (net)	17,262	20,272
All other	239	920
Total deductions	88,296	21,707
Net additions (+) deductions (−)	−87,611	−20,626
Assessments for expenditures of Board of Governors	−7,488	−7,330
Net earnings before payments to United States Treasury	940,456	1,253,357
Dividends paid	8,881	10,330
Payments to United States Treasury (interest on Federal Reserve notes)	923,936	1,212,926
Transferred to surplus	7,639	30,101
Surplus January 1	144,598	152,237
Surplus December 31	152,237	182,338

San Francisco Branch
P.O. Box 7702, San Francisco, California 94120

Los Angeles Branch
P.O. Box 2077, Terminal Annex, Los Angeles, California 90051

Portland Branch
P.O. Box 3436, Portland, Oregon 97208

Salt Lake City Branch
P.O. Box 30780, Salt Lake City, Utah 84125

Seattle Branch
P.O. Box 3567, Terminal Annex, Seattle, Washington 98124

Note: The graphics on pages 23-29 were prepared by Walter Thomason and Associates for wall displays in the assembly room of the Federal Reserve Bank of San Francisco. The graphics show persons and places associated with the history of each of the five geographic areas served by the San Francisco Reserve Bank.

Produced by William M. Burke, Vice President, Economic Information, and Karen B. Rusk, Manager, Publications and Graphics; Graphics designed by William Rosenthal, Graphic Artist; Federal Reserve Bank of San Francisco.