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Modest Growth in West for 1987 and 1988

Following the national pattern, the western region posted modest growth in 1987. Among the states that comprise the Twelfth Federal Reserve District, Arizona, California, Hawaii, Nevada, Oregon, and Washington grew as fast or faster than the nation. In contrast, Alaska, Idaho, and Utah experienced little or no growth.

The pattern of growth changed during 1987 as exports replaced consumer spending to become the driving force for the region's economy. The rate of growth in the West's retail sales slowed to a more moderate pace during 1987, and information from western retailers suggests that October's stock market turmoil has not affected that process significantly. At the same time, exports of many western products rose dramatically during the year, leading to increased production of many manufactured goods, agricultural products, and raw materials. Construction activity continued mixed in 1987, with nonresidential construction activity rising and homebuilding activity falling during the year.

Export-led growth

Throughout 1987, producers of goods for export benefited from the reduced foreign exchange value of the dollar as well as from overall strength in world markets and the increased use of more efficient technologies. In many cases, the value of exports of products in which the western states specialize rose even more rapidly than did the total value of U.S. exports.

The forest products industry was a major beneficiary of the falling dollar, and expanded production to a record level. The low foreign exchange value of the dollar, combined with strong building activity in Japan, boosted exports dramatically. The value of lumber and logs exported from the U.S. rose more than 30 percent between November 1986 and November 1987. Toward year-end, production was curtailed in parts of Oregon and Washington because drought-related fire danger briefly closed some forests to logging. Despite these problems, most indicators of activity in logs, lumber, paper, and plywood ended the year well above their year-end 1986 levels.

Rising exports also led to increased profitability for many western agricultural products. The value of cotton exports, many of them from California, doubled between 1986 and 1987. The value of vegetables, fruits, and nuts exported from the U.S. rose 12 percent. In addition, higher livestock prices improved the fortunes of western cattle producers.

Aluminum production also grew rapidly during 1987 as a combination of higher aluminum prices, lower labor costs, and a more favorable electric rate schedule recently negotiated with the Bonneville Power Administration made that production more profitable. These developments particularly helped the rural regions of Oregon and Washington where previously laid-off workers were re-hired.

Producers of electronic parts and data processing equipment saw improvements in their sales during 1987 as new products and the reduced value of the dollar stimulated demand. These improvements were translated into employment gains in many parts of the West, as well as increased demand for industrial space in California's Silicon Valley.

The aerospace and defense industries performed solidly in 1987 despite pressure on defense spending that reduced the value of 1986 Department of Defense contracts awarded to Twelfth District firms by almost 12 percent from the earlier year's level. Previously awarded contracts helped keep production from falling dramatically. Moreover, production of commercial aircraft continues to keep plants operating at capacity. For example, Boeing, buoyed by improved products and price competitiveness with its European rival Airbus Industrie, boosted exports of commercial aircraft during 1987 and currently has a backlog of orders more than three years long.

Slowing consumer spending growth

During 1987, the rate of growth in consumer spending fell, both nationally and in the West. For example, the value of retail sales in California, Oregon, and Washington combined grew

6.6 percent between the second quarter of 1986 and the second quarter of 1987; it grew slightly more slowly, at 4.9 percent, between the third quarters of those two years.

In some ways, slower growth in consumer spending is desirable. Rapid growth in consumption expenditures had been increasing consumers' debt burdens to worrisome levels, and also was fueling growth in the value of imported products, adding to the nation's trade deficit. Thus, slower consumer spending growth is expected to help bring consumer debt burdens and the value of imports down to more sustainable levels.

The turmoil in the financial markets during October led many to believe that consumers would retrench during the Christmas retail season. Some retailers, concerned about possible sharp consumer cutbacks, reduced prices more deeply and earlier this year than they did last year. Information currently available suggests that Twelfth District retailers posted modest sales growth, averaging little more than 5 percent, over the previous year's Christmas season.

Gains of this magnitude are in line with the pace of growth in consumer spending earlier in the year, and thus suggest that the uncertainty associated with the October 19 experience has not changed consumer spending patterns appreciably. However, aggressive price-cutting probably reduced some retailers' profit margins significantly.

Construction

The record of construction activity in the Twelfth District continues to be mixed. The value of nonresidential construction awards in the Twelfth District rose 10 percent from its 1986 level. In contrast, the number of residential construction permits fell about 15 percent. While the number of permits fell for both single-family and multifamily units, the drop was much greater for multifamily dwellings. This likely was due in part to changes in the tax code that make apartment buildings less attractive investments. In addition, a change in California building requirements that took effect on January 1, 1987 caused a surge in permits issued in that state during December 1986.

There also were significant differences across states in the amount of construction activity. Nevada, Oregon, and Washington saw improvements from 1986 in terms of more residential permits, nonresidential awards, and construction employment. For these states, strength in construction reflected overall economic health and, in the case of Oregon, a revival after the stagnation of the previous several years.

Alaska, Idaho, and Utah experienced deterioration or stagnation in all three measures of construction activity during 1987. By any measure, these three states had the weakest economies in the Twelfth District during 1987.

The other three District states — Arizona, California, and Hawaii — all experienced improvements in the value of nonresidential construction awards but deterioration in the number of residential permits. Hawaii and Arizona lost construction jobs during the year, while construction employment grew in California. These mixed signals are consistent with these states' healthy, but modest, economic growth rates.

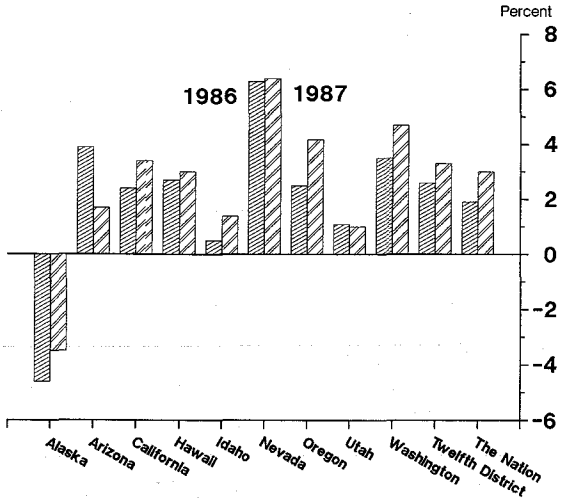
Energy and mining

The oil industry appears to have stabilized in 1987 after apparently cutting back too much in its adjustment to the sharp downturn in oil prices during early 1986. The oil industry's continuing problems were reflected most clearly in oil-dependent Alaska, where wage and salary employment fell 3.4 percent during 1987 after registering a 4.6 percent decline in 1986. Improvements in employment late in 1987, as well as increased rig counts from their year-earlier levels, suggest that Alaska's economy may be stabilizing at last.

Although the oil industry remains weak in California and Utah as well as in Alaska, Twelfth District producers continue to fare better than those in the nation's older oil producing regions. For example, oil production in Texas, Oklahoma, and Louisiana fell 14 percent between January 1986 and January 1988. In contrast, oil production in Alaska, California, and Utah remained constant during that period.

While oil production has stagnated, mineral mining has strengthened markedly during the

Nonagricultural Employment Growth in the West



past year. Prices of copper, gold, and zinc all rose substantially during 1987. In addition, technological improvements that substantially reduce the costs of recovering copper and gold have made mining of these metals much more profitable. In the Twelfth District, these improvements have benefited particularly parts of Idaho, Arizona, Utah, and Alaska.

Wages and prices

Nationally, the inflation rate rose slightly during 1987 as the Consumer Price Index (CPI) rose 4.4 percent, compared with a 1.0 percent increase during 1986, and the Producer Price Index (PPI) rose 2.1 percent, after a 2.3 percent decline in 1986. In the West, price increases appear to have been concentrated among metals, forest products, aluminum, and other basic resource or manufactured goods. Evidence suggests that wages rose more slowly than did the CPI, with increases for most western workers at or below the 3 to 4 percent range. Some regions and industries experienced outright wage declines.

Prospects for 1988

The pace of economic growth in the West is likely to slow during 1988, but information available at present suggests that the Twelfth District as a whole should avoid recession during the coming year. Strong demand and low inventories for many goods produced in the West, including forest products, aluminum, and aircraft, should support continued high production levels for these products. Growth in consumer spending is likely to continue at a slow pace. This will restrain growth, but also should allow consumers to work off their debt burdens and slow the demand for imports. Construction activity should remain mixed, as absorption of existing space makes room for additional profitable building.

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Editorial comments may be addressed to the editor (Gregory Tong) or to the author . . . . Free copies of Federal Reserve publications can be obtained from the Public Information Department, Federal Reserve Bank of San Francisco, P.O. Box 7702, San Francisco 94120. Phone (415) 974-2246.

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BANKING DATA—TWELFTH FEDERAL RESERVE DISTRICT

(Dollar amounts in millions)

Selected Assets and Liabilities Large Commercial Banks	Amount Outstanding 2/3/88	Change from 1/27/88	Change from 2/4/87 Dollar	Percent[7]
Loans, Leases and Investments[1 2]	203,473	− 147	4,916	2.5
Loans and Leases[1 6]	180,406	− 80	2,122	1.2
Commercial and Industrial	50,661	− 101	− 2,988	− 5.5
Real estate	70,660	55	4,038	6.0
Loans to Individuals	36,347	16	− 4,496	− 11.0
Leases	5,803	− 24	413	7.6
U.S. Treasury and Agency Securities[2]	16,034	− 58	2,530	18.7
Other Securities[2]	7,034	− 8	154	2.2
Total Deposits	202,830	3,839	− 2,219	− 1.0
Demand Deposits	50,332	2,623	− 2,229	− 4.2
Demand Deposits Adjusted[3]	34,243	1,704	− 13,629	− 28.4
Other Transaction Balances[4]	20,368	747	970	5.0
Total Non-Transaction Balances[6]	132,129	467	− 962	− 0.7
Money Market Deposit Accounts—Total	42,657	− 34	− 4,130	− 8.8
Time Deposits in Amounts of $100,000 or more	30,243	75	− 1,305	− 4.1
Other Liabilities for Borrowed Money[5]	22,704	− 1,026	− 5,664	− 19.9
Two Week Averages of Daily Figures	Period ended 1/25/88	Period ended 1/11/88		
Reserve Position, All Reporting Banks				
Excess Reserves (+)/Deficiency (−)	130	2		
Borrowings	11	20		
Net free reserves (+)/Net borrowed(−)	119	− 17		

1 Includes loss reserves, unearned income, excludes interbank loans
2 Excludes trading account securities
3 Excludes U.S. government and depository institution deposits and cash items
4 ATS, NOW, Super NOW and savings accounts with telephone transfers
5 Includes borrowing via FRB, TT&L notes, Fed Funds, RPs and other sources
6 Includes items not shown separately
7 Annualized percent change