

MONTHLY REVIEW

BUSINESS CONDITIONS IN THE TWELFTH FEDERAL RESERVE DISTRICT

Federal Reserve Bank of San Francisco

May 1, 1940

NEW business received by Twelfth District industries continued somewhat dull in March, and industrial operations declined moderately. As in other recent months, however, the aircraft, pulp and paper, and plywood industries maintained operations at capacity levels. Factory employment declined 3 percent, after allowance for seasonal influences, and payrolls decreased 5 percent.

In the field of consumption, retail sales of nondurable goods advanced in February and again in March. Sales of apparel and department stores increased more than seasonally, even after allowance for the early date of Easter this year. Sales of food shops and restaurants also increased, while drug store trade was higher than in any month in recent years and retail gasoline sales advanced moderately. New residential building expanded by the full seasonal amount, and preliminary data indicate an expansion considerably larger than usual in April, suggesting that sales of houses by builders are continuing at active levels. Furniture sales were slightly lower than in February. Automobile sales increased sharply, as is usual in March, and continued far above last year's levels.

INDUSTRY

The failure of industrial activity to expand by the full seasonal amount this spring may be attributed largely to the unseasonally high level of operations during the late fall and early winter months. To some extent, however, the growing scarcity of ships in the intercoastal trade has aggravated the situation in some important industries such as lumber and flour milling. It is estimated that of 149 ships operated as intercoastal carriers last September by 11 principal operators, 40 had been diverted to more profitable routes by March 25. The decline in available intercoastal capacity from 548,000 to 408,000 net tons has been reflected in sharply higher freight rates, with a resulting effect upon the competitive position of district producers in eastern markets.

New lumber orders advanced moderately from mid-February to mid-March, but displayed little net change during the following five weeks at a daily average rate of 39,900,000 board feet, compared with 36,400,000 board feet in January and February. Production did not increase by the customary seasonal amount in March, however, and unfilled orders rose slightly further. The failure of lumber output to advance seasonally may reflect partly the shortage of shipping space in the intercoastal traffic, referred to in the preceding paragraph. The maintenance of a good volume of orders for lumber is an outgrowth principally of the sustained high level of residential building in the Twelfth District and in other parts of the United States, since nonresidential building and export demand for lumber continue at low levels.

Moderate declines in output of motor vehicles and rubber tires took place in March, but steel mill output was relatively well maintained and furniture and cement production advanced. A major factor in the upturn in cement

output was the resumption late in February of deliveries to Grand Coulee Dam on which construction had been impeded by the weather.

Canning of spinach and asparagus was under way in April. The spinach crop was damaged by rain, and trade reports indicate that the total pack may not exceed the small 1939 output of 1,509,000 cases. The asparagus pack, which has been delayed rather than curtailed by adverse weather, will be restricted under the California Prorate Act to a maximum of 2,175,000 cases, compared with an average pack of 2,061,000 cases during the past five years. While current sales of canned and dried fruits, vegetables, and fish have been slow in recent weeks, carry-over stocks generally are small and the price structure is firm. Flour production displayed little change in March from the February level, and first quarter output was slightly lower than in the corresponding 1939 period.

AGRICULTURE

Heavy rain and snowfall during the first quarter of 1940 and in early April have resulted in generally favorable soil moisture conditions and prospects for summer irrigation water throughout most of the seven western states. This contrasts with last spring when shortage of soil moisture was widespread. The recent heavy rains caused considerable property damage in rural localities in California, but destruction of crops and livestock was not large. Growth of feed on livestock ranges has been excellent and growing conditions for most crops have been favorable this spring.

Although it is too early for production estimates of individual crops and of livestock and livestock products during the current season, present acreage and condition data suggest a total agricultural output in the district at least as large as in 1939. This may change as the season progresses, since important deciduous fruit crops are still subject to damage from late frosts, and spring sown grain and field crops on unirrigated lands are dependent to a considerable extent upon late rains.

The fall sown wheat crop, which can now be estimated fairly closely, is expected to be around 74,500,000 bushels, compared with 71,800,000 bushels harvested last year and an annual average production of 66,900,000 bushels during the ten years 1929-1938. Of this estimated total, the three Pacific Northwest states account for 56,100,000 bushels. The spring wheat crop in that area in recent years has ranged from 21,000,000 bushels to 58,000,000 bushels, largely depending upon abandonment of winter wheat acreage.

More wheat is grown in the Pacific Northwest than is consumed in that area, and much of the crop must be sold in other domestic or in foreign markets. Hostilities in Europe and the Orient have reduced export sales severely, and lack of cargo space has limited shipments by water to eastern and Gulf Coast ports of the United States. A considerable tonnage recently has moved by rail to mid-

western markets, however, where prices have been about 25 cents a bushel higher than in the Pacific Northwest. Prevailing prices to growers in the Northwest, while well below midcontinent quotations, are almost 40 percent higher than a year ago.

In California, the marketing of early spring lambs has been delayed this season. Growth of range forage was retarded by wet weather, and growers, anticipating abundant natural feed later in the season, held lambs for further weight gains before marketing them. Last spring, lack of rain and the resultant shortage of feed forced the early shipment of lambs from ranges, an unusually large proportion being sold for fattening. Quality of this year's lambs is excellent, and prices paid growers, as shown in the following table, have averaged higher than last year.

Sheep shearing became general throughout the district during March and April. As the quality and shrinkage of wool differs considerably, prices paid growers show a

LAMB PRICES RECEIVED BY CALIFORNIA PRODUCERS
(per hundred pounds)

Year	March 15	April 15	May 15	June 15	July 15	August 15
5-Yr. Av. (1934-38)	\$8.38	\$8.18	\$7.48	\$7.40	\$7.24	\$6.84
1938	8.00	7.80	6.50	6.50	6.60	6.60
1939	8.00	7.80	7.90	7.80	7.50	6.80
1940	8.60	9.00

wide variation in different sheep-raising areas of the district. Quotations for clips have ranged from 22 to 38 cents per pound this spring and have averaged about 25 percent higher than a year ago. The number of sheep to be shorn this season is about the same as last year.

BANKING AND CREDIT

Earning assets of all member banks declined considerably in the first quarter of 1940, but in late March they were substantially higher than a year earlier. About half of the decrease of \$29,860,000 in loans during the first quarter, shown in the accompanying table, occurred at banking offices located in the principal district cities. At these offices, declines were reported in loans for purchas-

ing or carrying securities, in advances on real estate, and particularly in the "all other" classification, while advances for commercial, industrial, and agricultural purposes increased slightly further. Compared with a year earlier, loans outstanding increased \$87,288,000. This rise was accounted for entirely by offices located outside the larger cities.

EARNING ASSETS OF ALL MEMBER BANKS—TWELFTH DISTRICT
(in thousands of dollars)

	Mar. 26, 1940	Change from— Dec. 30, 1939	Mar. 29, 1939
Loans and discounts	1,937,008	-29,860	+ 87,288
United States Government obligations	1,382,462	-67,648	+ 61,139
Obligations of states and political subdivisions	387,714	+ 5,302	+ 53,178
Other securities	138,662	- 3,357	- 16,845
Total loans and investments	3,845,846	-95,563	+184,760

The decrease of \$65,703,000 in securities held by member banks in the Twelfth District during the first three months of 1940 reflected a sharp reduction in investments in Government obligations held by city banks. Sales of these securities were made after prices had risen considerably from the levels to which they had fallen immediately after the outbreak of war in Europe, although at no time in recent months have they been as high as in the early summer of 1939.

During the month of April loans of member banks in the principal district cities fluctuated with little net change, but investments continued the decline noted during the first quarter.

The recent liquidation of securities involved transfer of the proceeds to this district from eastern markets and had an important influence in expanding local bank reserves to the highest levels on record. Since the beginning of the year, reserves have risen by \$130,899,000 and on April 24 totaled \$714,492,000.

Distribution and Trade—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment (1940-1939)			Without Seasonal Adjustment (1940-1939)		
	Mar.	Feb.	Mar.	Mar.	Feb.	Mar.
Retail Trade						
Department store sales (value)*						
Twelfth District	102	99	99	95	83	89
California	99	97	99	94	83	90
Los Angeles	89	89	93	85	78	85
Bay Region	107	102	105	101	85	93
San Francisco	98	93	98	92	80	87
Oakland	131	125	124	123	100	110
Pacific Northwest	105	103	99	95	81	86
Portland	102	107	101	95	89	91
Seattle	108	103	100	96	78	85
Spokane	102	93	91	89	68	74
Salt Lake City	97	88	87	85	70	74
Department store stocks (value)†	63	64	65	64	62	67
Furniture store sales (value)*‡	79	81	73	71	73	65
Furniture store stocks (value)‡	74	74	68	74	71	68
Automobile sales (number)*						
Total				119	101	95
Passenger				112	95	88
Commercial				188	163	166
Carloadings (number)*						
Total	86	91	79	80	75	74
Merchandise and misc.	95	99	93	88	82	87
Other	76	81	62	70	66	58
Intercoastal Traffic (volume)						
Total	70	77	69	69	69	68
Eastbound	56	75	57	52	61	53
Westbound	120	104	110	127	94	116

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

Production and Employment—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment (1940-1939)			Without Seasonal Adjustment (1940-1939)		
	Mar.	Feb.	Mar.	Mar.	Feb.	Mar.
Industrial Production*						
Manufactures (physical volume)						
Lumber	82	90	69	77	70	64
Refined oils	—	—	—	158	155	153
Cement	107	94	101	108	83	102
Wheat flour	121	119	121	118	119	118
Minerals (physical volume)						
Petroleum	—	—	—	92	92	94
Lead (U. S.)†	82	78	69	83	81	70
Silver (U. S.)†	..	103	86	..	111	94
Construction (value)						
Residential building permits‡						
Twelfth District	58	57	54	67	51	62
Southern California	61	64	63	70	56	71
Northern California	50	42	42	61	45	51
Oregon	37	41	22	54	39	32
Washington	56	57	39	64	47	45
Intermountain states	117	104	94	104	49	83
Public works contracts	—	—	—	116	191	140
Miscellaneous						
Electric power production	231	228	210	215	209	196
Factory Employment and Payrolls§						
Employment						
Pacific Coast	121	124	104	118	116	102
California	137	137	116	133	131	113
Oregon	106	111	101	102	100	97
Washington	97	104	84	96	96	83
Payrolls						
Pacific Coast	117	124	99	117	114	101
California	131	137	110	133	129	111
Oregon	99	106	95	95	94	92
Washington	96	105	78	96	95	78

*Daily average. †Prepared by Board of Governors of Federal Reserve System. ‡Includes figures from 197 cities and Los Angeles County, unincorporated. §Excludes fish, fruit, and vegetable canning.

Operating Ratios of Member Banks—1939

The study of operating ratios of Twelfth District member banks prepared annually by this bank has recently been completed for the year 1939. This analysis shows that net profits of member banks in this district again averaged well above 8 percent on total capital accounts, which consist of paid in capital, surplus, undivided profits, and reserves for contingencies. The 1939 figure of 8.6 percent is the same as the average rate of net profits in 1938 but somewhat below the 1937 average of 9.3 percent. These averages, it should be noted, are not based upon aggregate dollar figures covering all banks, but are averages of the ratios for individual banks. That is, the rate of profit was first computed for each bank, and those percentages were then averaged. In this way, large banks had no more weight in the average than small banks. This method was used in order to show the average bank performance, rather than that of the banking system as a whole.

Banks serving the more sparsely populated states generally showed higher rates of profits than those operating in metropolitan localities. For example, banks in Arizona averaged 14.2 percent; in Nevada, 12.1 percent; and in Idaho 10.5 percent; while the lowest state average of net profits on invested capital, 6.7 percent, was shown by the 113 member banks in California. The 14 banks which have deposits of more than \$50,000,000, and which extend the bulk of credit in the district, showed lower net profits than most other groups, averaging 7.1 percent on invested capital. Of these 14 banks, 10 are located in California and their net profits averaged 6.0 percent. The other four, located in the Pacific Northwest, showed net profits averaging 9.9 percent on invested capital. Cash dividends averaged 3.5 percent of total capital funds during 1939.

Income from loans made up a larger proportion of total operating income in 1939 than in 1938, averaging 61.1 percent in the later year. Loans represented about the same percentage of total assets in 1939 as in 1938, but comprised a larger proportion of earning assets than in the previous year. Income from securities declined in importance, owing to the smaller proportion of assets employed in that manner. Service charge income increased further, averaging 5.5 percent of total earnings in 1939.

Current operating expenses of banks took, on the average, 71.5 percent of total income, compared with 71.2 percent in 1938. The increase resulted entirely from relatively higher salary and wage costs inasmuch as interest paid on deposits declined, and taxes and other expenses absorbed the same proportion of gross earnings in 1939 as in 1938. After meeting all current operating costs, but before charge-offs because of losses and depreciation, banks showed smaller net earnings in 1939 than in 1938, both in relation to total operating earnings and to total capital funds. A considerably smaller proportion of earnings was used for charging off losses and depreciation on loans, securities, and other assets, however, and the proportion of total operating income retained as net profits increased to 24.8 percent, compared with 23.6 percent in 1938. Since dividend payments took an average of 10.3 percent of total operating income, 14.5 percent of operating income remained for capital enhancement.

Even with substantial additions to capital funds from undistributed earnings, the average ratio of capital funds to deposits declined, owing to the rapid growth in deposits. The average ratio of capital funds to assets subject to depreciation probably showed little or no decrease, however, since a substantial part of the additional deposits was not invested but was held as cash in vault or as deposits in the Federal Reserve Bank.

OPERATING RATIOS OF MEMBER BANKS—TWELFTH DISTRICT
(Arithmetical averages of individual bank ratios, rather than ratios based upon aggregate dollar amounts)

	Grouped According to Volume of Deposits												All Banks 1938 1939	
	Under \$500,000		\$500,000 to \$1,000,000		\$1,000,000 to \$5,000,000		\$5,000,000 to \$25,000,000		Over \$25,000,000					
	1938	1939	1938	1939	1938	1939	1938	1939	Branch 1938 1939	Nonbranch 1938 1939	1938	1939		
Number of Banks . . .	65	58	87	82	81	83	39	39	10	11	3	3	285	276
Percentages of Total Current Earnings														
SOURCES OF EARNINGS														
Int. and discount on loans . . .	64.8	66.6	60.9	62.2	58.9	61.0	52.9	54.8	55.0	56.2	34.5	31.1	59.6	61.1
Int. and div. on securities . . .	19.7	17.5	24.8	22.9	25.6	24.1	26.1	24.8	26.5	26.2	52.4	56.4	24.4	22.9
Service charges	5.6	6.0	5.3	5.8	5.1	5.3	5.0	5.1	5.0	5.2	0.6	0.6	5.2	5.5
All other earnings	9.9	9.9	9.0	9.1	10.4	9.6	16.0	15.3	13.5	12.4	12.5	11.9	10.8	10.5
Total earnings	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
DISPOSITION OF EARNINGS														
Salaries and wages	32.7	34.5	29.9	30.3	30.1	30.6	30.0	30.3	32.9	32.9	23.8	23.9	30.7	31.3
Interest on deposits	13.0	14.0	18.2	17.5	17.6	17.2	19.3	18.1	16.9	16.8	23.0	20.8	17.0	16.7
Taxes	5.3	5.1	5.2	5.1	4.9	5.2	5.6	5.6	4.3	4.8	7.8	7.6	5.2	5.2
Other	19.5	19.8	17.9	18.1	17.9	17.2	18.4	18.3	19.1	19.3	13.7	13.2	18.3	18.3
Total expenses	70.5	73.4	71.2	71.0	70.5	70.2	73.3	72.3	73.2	73.8	68.3	65.5	71.2	71.5
Net current earnings	29.5	26.6	28.8	29.0	29.5	29.8	26.7	27.7	26.8	26.2	31.7	34.5	28.8	28.5
Net charge-offs	8.0	2.4	4.5	5.3	4.8	2.3	3.3	3.5	2.0	5.7	13.1	14.1	5.2	3.7
Net profits	21.5	24.2	24.3	23.7	24.7	27.5	23.4	24.2	24.8	20.5	18.6	20.4	23.6	24.8
Percentages of Total Capital Funds														
Net current earnings	10.2	8.9	10.7	10.5	11.3	11.3	10.2	10.2	10.3	9.5	11.3	12.3	10.7	10.3
Net charge-offs	2.9	1.3	2.0	2.3	2.0	1.4	1.5	1.3	0.7	2.5	4.6	5.1	2.1	1.7
Net profits	7.3	7.6	8.7	8.2	9.3	9.9	8.7	8.9	9.6	7.0	6.7	7.2	8.6	8.6
Cash dividends declared	3.2	3.3	3.4	3.5	3.6	3.4	3.4	3.5	4.4	3.7	6.4	6.3	3.4	3.5
Percentages of Total Loans														
Int. and disc. on loans	7.5	7.3	6.9	6.8	6.4	6.4	5.5	5.3	5.0	5.0	3.9	4.0	6.6	6.6
Percentages of Total Securities														
Interest and div. on sec.	3.7	3.7	3.4	3.4	3.3	3.3	2.8	2.7	2.5	2.3	2.8	2.5	3.4	3.4
Profits on securities sold	0.4	1.2	0.9	0.8	0.6	0.9	0.9	0.8	1.0	1.1	0.1	0.3	0.7	0.9
Capital Ratio														
Capital funds to tot. deposits	18.8	18.9	15.2	14.9	13.7	13.0	11.1	10.9	9.5	9.6	8.5	7.6	14.8	14.3

Summary of National Business Conditions

Prepared by the Board of Governors of the Federal Reserve System

INDUSTRIAL activity continued to decline during March but at a somewhat slower rate than in the preceding two months, and in the first half of April there was little further decrease. Wholesale prices of basic commodities decreased somewhat in the latter half of March but recovered by the middle of April. Distribution of commodities to domestic consumers continued in large volume, and exports were at the high levels reached last December.

PRODUCTION

The Board's index of industrial production, which is adjusted for usual seasonal variations and for the number of working days, was 103 in March compared with 109 in February. The decline reflected chiefly a further reduction in output of steel and considerable decreases in activity at cotton and woolen textile mills.

Steel ingot production declined from an average of 69 percent of capacity in February to an average of 64 percent in March. In the first half of April output was at around 61 percent of capacity. Automobile production in March and the first half of April was maintained at the high rate prevailing during January and February but did not show the increase customary at this season. Retail sales of automobiles continued in large volume, and dealers' stocks of new cars declined somewhat from the high level reached earlier. In the machinery industries activity showed some decline from the high rate of other recent months, while at aircraft factories and shipyards activity continued at peak levels. Output of lumber and plate glass advanced seasonally in March.

In the woolen textile industry, where activity had been declining from the high level reached last November, there was a further sharp reduction in March. Activity at cotton textile mills also declined considerably but remained at a somewhat higher level than prevailed a year ago. Shoe production likewise declined considerably in March. At silk mills activity remained at an exceptionally low level, while rayon production was large.

Mineral production was maintained in large volume in March. There was some further reduction in output of bituminous coal, but output of anthracite increased, following a sharp decline in February. Crude petroleum production continued at record levels.

Value of construction contracts awarded, as reported by the F. W. Dodge Corporation, increased considerably in March, as is usual at this season. The increase was principally in awards for private work, which in March approximately equalled those in the corresponding period last year. Public awards increased somewhat, following declines in January and February, but were in smaller volume than a year ago. Private residential building rose by about the usual seasonal amount.

DISTRIBUTION

Sales of general merchandise at department and variety stores and by mail-order houses increased by about the usual seasonal amount from February to March, with allowance for the earlier date of Easter this year. In the first week of April sales at department stores were at a higher level than in March.

Freight-car loadings showed little change from February to March, although a rise is usual between these months. Shipments of miscellaneous freight showed considerably less than the usual season increase, and there was some further decline in loadings of coal.

FOREIGN TRADE

Exports of United States merchandise in March continued near the high level reached last December. Agricultural exports, principally cotton, decreased from February to March, while there were substantial increases in shipments of commercial vehicles and in metal working, agricultural, and other types of machinery.

During March, the country's monetary gold stock increased by \$256,000,000. In the first two weeks of April the rate of gold inflow was accelerated, acquisitions in this period amounting to \$145,000,000.

COMMODITY PRICES

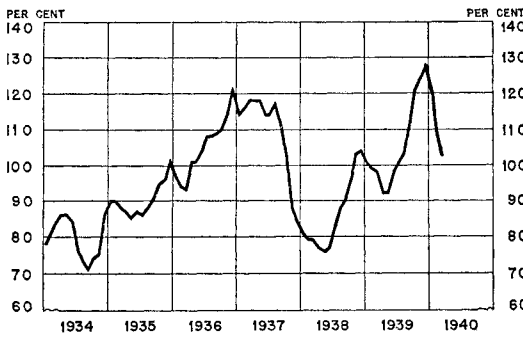
Prices of a number of basic agricultural and industrial commodities, which had declined in the latter part of March, advanced during the second week in April. Prices of certain finished steel products, on the other hand, were reduced, and prices of most other commodities showed little change.

GOVERNMENT SECURITY MARKET

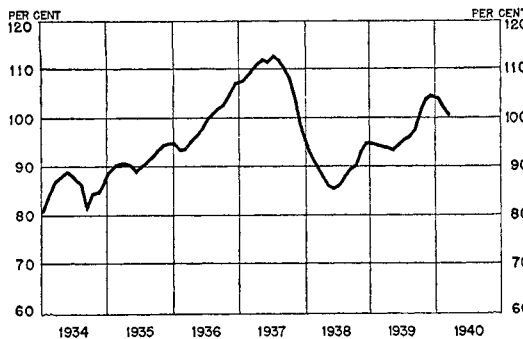
Prices of Treasury bonds moved sharply upward during March and the first few days of April to a new high level since last summer. On April 9, however, on receipt of news of the expansion of war activities in Europe, a decline of about one point occurred in long-term bonds. Subsequently the market recovered part of the loss. The yield on the 1960-1965 Treasury bonds was 2.31 percent on April 15, compared with a low of 2.26 percent on April 2.

BANK CREDIT

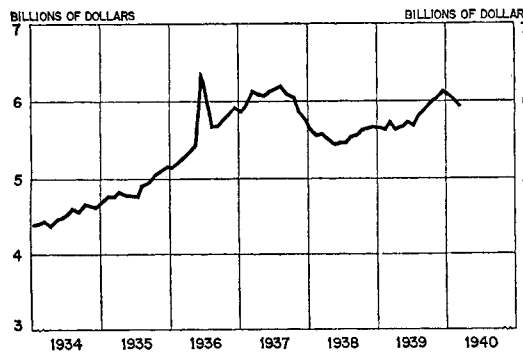
Reflecting continued heavy gold imports, excess reserves of member banks increased during the four weeks ending April 10 to a record high level of \$5,950,000,000. Total loans and investments at banks in 101 leading cities, which had shown little net change during March, increased in the first two weeks of April, reflecting purchases of United States Government obligations.



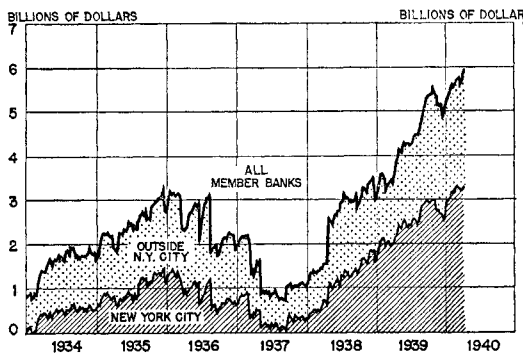
INDUSTRIAL PRODUCTION
Index of physical volume of production, adjusted for seasonal variation, 1923-1925 average=100. By months, January 1934 to March 1940.



FACTORY EMPLOYMENT
Index of number employed, adjusted for seasonal variation, 1923-1925 average = 100. By months, January 1934 to March 1940.



INCOME PAYMENTS
United States Department of Commerce estimates of the amount of income payments to individuals, adjusted for seasonal variation.



EXCESS RESERVES OF MEMBER BANKS
Wednesday figures partly estimated, January 3, 1934, to April 13, 1940.