

MONTHLY REVIEW

BUSINESS CONDITIONS IN THE TWELFTH FEDERAL RESERVE DISTRICT

Federal Reserve Bank of San Francisco

November 1, 1941

VIEWED over the first nine months of the year, a large expansion has taken place in Twelfth District industrial production and employment. Expansion, although still continuing, was less pronounced in August and the retarded rate of increase was somewhat more evident in September. In the field of construction, value of permits issued for private residential building decreased in September for the second successive month, although some seasonal expansion is customary at this time of year, and the value of nonresidential building was also lower. Preliminary data for October, however, indicate a smaller than seasonal decline in private residential construction. Retail trade was somewhat less active than in the preceding month, seasonal influences considered, but the decline was from an unusually high level.

Activity in local defense industries, centering principally about aircraft production and shipbuilding, expanded further in September, while operations in other major district industries were generally well maintained. Lumber production in September, after allowance for seasonal influences, was about unchanged from the previous month, a small decline in output in the Douglas fir region approximately offsetting an increase in the western pine area. For the second successive month, new orders received by mills decreased and were smaller than output. Prices for Douglas fir have weakened recently, quotations for several items declining below the ceiling established by the Office of Price Administration, effective October 1. Output of crude petroleum was about unchanged in September, but refinery operations declined slightly. Mining and smelting of non-ferrous metals continued highly active with encouragement to further expansion in zinc output provided by action of the OPA in raising the ceiling price of this metal from 7.25 cents to 8.25 cents per pound in October. Pulp production in the Pacific Northwest continued unabated at effective capacity.

Early in October the Supply Priorities and Allocations Board recommended that annual steel producing capacity in the United States should be increased by 10,000,000 tons. The report on which the recommendation was based indicated that for strategic reasons it would be desirable to make the West Coast substantially independent of eastern mills for its steel supply. Under plans previously submitted by Coast steel producers, production in the Twelfth District would be approximately tripled. On Oc-

tober 22, the Defense Plant Corporation announced the execution of a lease agreement with a western steel concern for construction of a \$35,000,000 pig iron plant in Utah. Two days later the OPM formally recommended that the Defense Plant Corporation finance a \$36,000,000 steel plant in California for the production of plates and castings.

While activity in defense industries expanded, and output of the other major district industries was well maintained, there was some evidence in September and early October that operations and employment in a number of small plants using metals but manufacturing products not essential for defense had been curtailed because of lack of materials. Total factory employment and payrolls in Pacific Coast states, however, increased further in September, allowing for customary seasonal influences.

Retail trade, as measured by department store sales, declined in September on a seasonally adjusted basis. This decline, however, followed the sharp increase in sales in the preceding month. The abrupt August increase in consumer buying reflected fears of shortages, particularly of items containing silk, and was also induced by the announcement of regulations, effective September 1, designed to curb installment buying. Department store sales of major household appliances, which had risen markedly in August, declined in September but showed a larger year period gain than in any month other than August. In September, consumers actively purchased goods such as radios, furs, jewelry, and liquors on which new Federal taxes became effective on October 1. Department store sales of furs, for example, were more than twice as large as in September 1940. New passenger car sales declined in September to the lowest figure for any month since 1938. Part of this decrease may reflect the fact that 1942 models were not in dealer hands throughout the month, but trade comment indicates fairly widespread buying indifference in recent weeks. Prices of new cars are higher, and the active buying during the past model year may, in part, have represented sales "borrowed" from the present model year. Provisions of the regulation of consumer installment credit, the most important of which relate to the size of the minimum down payment and the maximum length of time over which contracts may be written, adopted by the Board of Governors of the Federal Reserve System effective September 1, were also a factor.

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Priority Unemployment

The threat of depressed areas marked by idle men and closed plants resulting from the inability of certain industries to obtain materials shows few signs of materializing in the Twelfth District, although an increasing proportion of supplies is being diverted from ordinary uses to defense as priority regulations and allocations are extended. Individual dislocations have occurred and will continue to occur, and the future course of employment in particular plants is uncertain, but layoffs of men and plant shutdowns have so far been of proportions in no way indicating the development of depressed areas.

The relatively fortunate position of the district in this respect is occasioned by two factors. The first is the comparative unimportance of vulnerable industrial activities in the economy. The second is the distribution of those activities, which are, for the most part, located in industrial areas where defense production continues to expand.

National attention has been directed primarily toward consumer goods industries which use scarce materials and toward the communities in which those industries are dominant sources of employment. In this district, however, such industries are not a large part of the total and there are no communities dependent primarily upon them as is the case in certain other sections of the country, notably the Middle West. Automobile assembly plants employ a considerable number in California and the manufacture of heating equipment is of some im-

portance throughout the district, but the manufacture of silk products, aluminum ware, refrigerators, washing machines, vacuum cleaners, metal furniture, and other products using scarce materials, although represented, is not extensive. Altogether, employment in consumer goods industries which might be affected, is about three percent of total factory employment in the district.

The trend of employment in automobile assembly plants, which hire the largest number of workers among the vulnerable consumer goods industries in the district, has been uncertain in recent weeks. Drastic layoffs on account of shortages of materials and parts have not yet occurred, but rehiring after the changeover to new models, although substantial, did not raise employment to the high level reached in the summer prior to the end of the model year. Both the partial conversion of plants to defense production and their proximity to defense industries, however, should prevent significant unemployment in the areas where such plants are located even if automobile production should be restricted more severely in the future.

Small metal-working shops are being affected, and construction employment may be curtailed as non-defense building and other construction projects are restricted, but many of the workers in those fields have skills which will enable them to shift more or less readily to defense employment. Some distributors, particularly small retailers, are faced with the necessity of reducing their staffs because of inability to maintain stocks.

Whether or not the problem of so-called priority unemployment will reach imposing proportions throughout the country in the future depends upon the demands of defense, the distribution of defense contracts, the extent to which labor and other resources released from non-essential employment can be shifted into emergency activities, and the development of substitute materials. In evaluating the effects of these factors in the Twelfth District, it must be remembered that a major part of the non-agricultural resources of the area is devoted to the production of copper, lead, and zinc, so-called strategic materials; lumbering; petroleum production and refining; fruit, vegetable, and fish canning; and motion picture production. None of these activities have been restricted appreciably by the defense program; for the most part they have increased under its impetus. At the same time the industrial areas on the Pacific Coast are the scene of continuing rapid expansion in aircraft production and shipbuilding which have already attained the status of major sources of employment in the district.

Production and Employment—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment—			Without Seasonal Adjustment—		
	1941 Sept.	1940 Aug.	1940 Sept.	1941 Sept.	1940 Aug.	1940 Sept.
Industrial Production¹						
Manufactures (physical volume)						
Lumber	108	108	92	126	129	107
Refined oils	—	—	—	176	189	167
Cement	180	169	124	191	189	132
Wheat flour	106	98	105	126	98	125
Minerals (physical volume)						
Petroleum	—	—	—	98	97	93
Lead (U. S.) ²⁻³	116	112	..	116	112
Silver (U. S.) ²	125	109	..	129	107
Copper (U. S.) ²⁻³	154	155	137	152	152	136
Construction (value)						
Residential building permits ⁴						
Twelfth District	75	87	65	83	87	72
Southern California	71	92	69	78	90	76
Northern California	73	67	54	79	65	59
Oregon	39	55	58	46	55	69
Washington	111	137	61	120	158	66
Intermountain states	133	106	91	175	118	120
Public works contracts	—	—	—	373	419	294
Miscellaneous						
Electric power production	248	264	230	259	289	241
Factory Employment and Payrolls⁵						
Employment						
Pacific Coast	188	180	129	196	185	135
California	225	217	148	233	224	154
Oregon	136	132	107	147	138	116
Washington	141	130	103	148	133	108
Payrolls						
Pacific Coast	239	225	136	248	236	140
California	284	269	158	289	279	160
Oregon	160	160	105	178	178	116
Washington	186	167	105	197	176	111

¹Daily average.

²Prepared by Board of Governors of the Federal Reserve System. (1935-1939 = 100).

³Seasonal factors revised.

⁴Includes figures from 197 cities and Los Angeles County, unincorporated.

⁵Excludes fish, fruit, and vegetable canning.

Distribution and Trade—

Index numbers, 1923-1925 average=100	With Seasonal Adjustment—			Without Seasonal Adjustment—		
	1941 Sept.	1940 Aug.	1940 Sept.	1941 Sept.	1940 Aug.	1940 Sept.
Retail Trade¹						
Automobile sales (number) ²						
Total	—	—	—	..	118	84
Passenger	—	—	—	..	53	104
Commercial	—	—	—	..	270	170
Carloadings (number) ²						
Total	103	102	89	118	118	102
Merchandise and misc.	114	112	96	134	126	113
Other	89	89	80	99	107	89

¹Department and furniture store indexes, customarily shown in this table, are in the process of revision.

²Daily average.

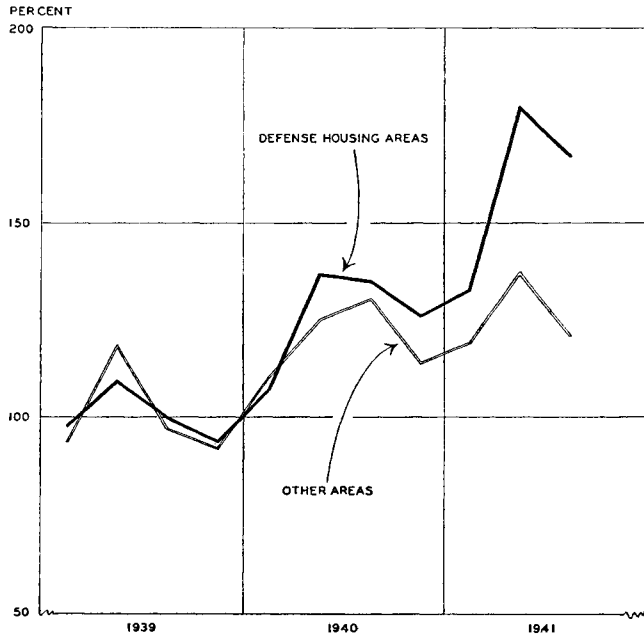
**Private Residential Building
in Defense and Non-Defense Areas**

New private residential building declined in August and September, although a substantial seasonal increase is customary in those months. This decline was from the unusually stable and high levels of the preceding four months to which new private residential building had pressed forward in the second half of 1940 and early 1941. Preliminary data for October indicate, however, that value of permits for this class of building will not show any large change from the September total, although a substantial seasonal decline is usual.

Expansion in dwelling construction in late 1940 and early 1941 largely reflected efforts to meet sharply increasing demand for housing near defense industrial centers and important military and naval bases. In a press release dated September 19 the OPM announced a list of localities (shown on page 56) which it has classified as critical defense housing areas, and the marked increase in value of private residential building permits in these areas as a group in 1940 and particularly in the first half of 1941 is shown in the accompanying chart. The chart also indicates that the increase in new residential building in other areas, referred to in this discussion as non-defense areas, was much more moderate.

The August-September downturn in new residential building was common to both defense and non-defense areas, classified on the basis indicated in the preceding paragraph. In the district as a whole, about the same percentage decline occurred in both categories, but on a regional basis some variation was apparent. This variance is shown in the accompanying table, which compares average monthly valuation of building permits issued in August and September with those issued in April-July, inclusive. The percentage figures shown in the table represent the aggregate change in residential building. Changes for many cities varied considerably from the average. For example, Bakersfield and Stockton are both classified as defense housing areas in the northern California region, yet the monthly average values of new dwellings started in these cities were 17 and 47 percent lower in the later period than in the preceding four months.

vate residential building. The demand for skilled labor in industrial construction and in shipyards has resulted in a decreased labor supply available for home building, a more rapid turnover of employees, and the utilization of less efficient labor. Many smaller contractors as well as workmen have shifted to industrial employment. Building costs have risen. Not only have the costs of materials and labor advanced, but uncertainty over the availability of labor and materials has caused an increasing number of contract builders to build only on a cost plus basis or to include a considerable margin of safety in their bid prices. Uncertainty over the length of the construction period itself has been a deterring factor for both operative builders and owner-builders.



NEW PRIVATE RESIDENTIAL BUILDING—Twelfth District
Indexes of permit valuation, not adjusted for seasonal variation, 1939 average=100. By quarters, January 1939 to September 1941.

NEW PRIVATE RESIDENTIAL BUILDING—TWELFTH DISTRICT
August-September average compared with April-July average, 1941
Percent change in Value of Permits

Region	Defense Housing Areas	Other Areas	Total	Average Seasonal Change
So. California.....	-16	-13	-15	-1
No. California.....	-11	-8	-10	-4
Oregon.....	-20	-32	-23	-3
Washington.....	-3	-34	-7	-7
Intermountain.....	7	+3	3	-7
Twelfth District.....	-13	-12	-13	-2

General attention has been directed to the restriction upon residential building that is expected to follow the recently established priorities on critical building materials, but, as indicated above, there is evidence that a decline was already under way in most parts of the district before action in regard to priorities was taken. The purpose of the housing priority order was to obtain a more efficient distribution of the critical metals and metal products used in housing. Shortages of these materials were not solely responsible for the recent decline in pri-

Decreasing availability of credit has been another factor in the situation. Although interest rates have not risen and terms of repayment have been made no stricter (installment credit controls of the Board of Governors of the Federal Reserve System do not apply to loans secured by improved real estate), appraisals, both of the FHA and of private lending agencies not making insured loans, have not risen to an extent comparable with costs. In part this is a typical lag, but the FHA in its valuations has not recognized the increase in costs since the inception of the defense program except in a very few areas in which such changes have been considered to reflect more permanent conditions. The result has been to discourage potential borrower-builders since the ratio of loan to cost has declined. With operative builders, the fact that there is considerable buyer resistance to a price above the appraised value has also played a part. Uncertainty over the possibility of rent controls, the permanence of population shifts (a landlord cannot amortize his "plant" for tax purposes in five years), and the level of building costs after the emergency is over also may have had some effect.

The requirements for housing in the district in the

immediate or near-term future are indeterminable at this time. The population of many defense areas is still increasing, but the rate of increase probably has declined in some districts and may do so before long in others. As the influx of workers declines, the need for additional housing also falls off. A related factor is the likelihood that to a greater extent than in the past, further gains in defense employment will take place through the transfer of workers from local non-defense employment and through the hiring of persons, including women, not normally engaged in gainful occupations within the community.

As far as governmental restrictions upon the availability of building materials are concerned, it should be clearly recognized that, although priorities on critical housing materials affect their distribution as between defense and non-defense housing, the more basic factor which necessitates such restriction is the competition for metals between construction on the one hand and industrial and armament production on the other. Thus the interpretation of the comparative needs of those two types of activities by SPAB and the Priorities Division of the OPM will be the fundamental factor in the distribution of critical building materials.

Priority regulation of critical building materials for defense housing, announced by the Priorities Division of the OPM, went into effect on September 22. Under this regulation, a builder, upon approval, is given a project preference rating which may be used in his purchases of critical building materials for that project. A rating is not in itself a guarantee of delivery, nor is the absence of a rating a prohibition of purchase, although the difficulty of replenishing stocks may deter sales by dealers to buyers without ratings, since a dealer can extend a buyer's rating to his own purchases. The holder of a priority rating merely has a claim ahead of those with lower ratings or no rating who may have orders pending or who may be seeking to purchase at the same time.

Highest ratings are to be given to projects under construction as of September 1 and to remodeling and rehabilitation. Lower ratings are to be given new construction for rent, and still lower ratings to new construction for sale. Urgency with respect to time and location will also affect the rating granted.

Preference ratings apply only to those building materials on the defense housing critical list, which is limited almost entirely to metal and metal products, not to all building materials. Steel and iron products, plumbing and gas distribution systems, heating and ventilating equipment, certain metal household equipment, electrical supplies, and land development items such as pipe lines make up the list. Lumber and cement are not included.

To be granted a rating, the proposed construction must be located in a defense housing critical area, and must be intended primarily for defense workers. The estimated market price is not to exceed \$6,000 nor can the proposed rental exceed \$50 per month per family unit. To economize on scarce materials, approval is further conditional upon plans calling for the use of minimum quantities of metals. In this connection, SPAB has asked that building codes be altered wherever such action would eliminate the otherwise unnecessary use of those materials.

In the Twelfth District, the following areas, whose outer limits are defined in terms of reasonable commuting distance from defense employment, have been so designated.

California	Washington	Idaho
Bakersfield	Bremerton	Boise
Fresno	Everett	
Los Angeles	Keyport	Nevada
Monterey	Longview-Kelso	Hawthorne
Oceanside-Fallbrook	Seattle	Las Vegas
San Diego	Spokane	
San Francisco and	Tacoma	Utah
East Bay Cities		Ogden
San Luis Obispo	Oregon	Salt Lake City
San Miguel-Paso Robles	Astoria	
Stockton	Hermiston	Arizona
Vallejo	Pendleton	Litchfield Park
	Portland	

Although the OPM priority regulation of critical building materials is being applied to housing only, on October 9 the SPAB issued a statement of policy indicating that no public or private construction projects of any sort which use appreciable quantities of critical materials, may be started during the emergency unless they are necessary either for national defense or essential to public health and safety.

Agriculture

Prices paid farmers for their products in the United States advanced substantially in the six months ending in mid-September but about that time the continuous increase in the average of these prices was halted, temporarily at least. In general, these prices fluctuated during the following month slightly below the level prevailing in mid-September. At that level they averaged 40 percent higher than a year earlier and higher than at any time since 1930. This average for the first time in the past 21 years, exceeded the average of prices farmers paid for the items they purchase, including taxes and interest on indebtedness.

Farm products produced in considerable volume in this district which showed the largest price advances over a year ago in mid-September included cotton, cottonseed, wheat, barley, eggs, flaxseed, butter, deciduous fruits sold fresh to consumers, and sheep and lambs. Products which showed more moderate but nevertheless substantial gains over the period included apples, cattle, chickens, corn, hay, potatoes, sweet potatoes and most other vegetables, citrus fruit, prunes and walnuts. Prices paid United States farmers for both cotton and cottonseed have risen steadily since early this year, and in mid-September were higher than at any time in the last decade. Notwithstanding record or near-record crops of most grains, farm prices of grains as a group averaged over 37 percent above those of September 1940. Although the production of milk, cheese, and butter are at record levels and September 1 stocks of butter and cheese were 49 and 29 percent, respectively, larger than on September 1, 1940, farm prices for all principal dairy products advanced more than seasonally during the following month. At 140 percent of the 1909-1914 level in mid-September, dairy products prices averaged over 26 percent higher than a year earlier and were higher than in any other September since 1929. The index of citrus and deciduous fruit prices, after reaching 100 percent of the 1909-1914 base in August, declined to 89 percent in September. This was the only group of farm products selling at lower prices than in the 1909-1914 period.

Exports of farm products from the United States, which had been severely curtailed as a result of war developments, have recently revived under the impetus of the lend-lease program. From September 1940 through January 1941 exports were at an annual rate of about \$240,000,000, but in June they had risen to an annual rate of some \$740,000,000. At this level, they approximate the average of recent years, but are considerably below the average of the 1920's.

AGRICULTURAL PRODUCTION—TWELFTH DISTRICT
(in thousands of units)

	Average 1930-39	1939	1940	Indicated 1941
Grain and Field Crops				
Barley (bu.)	42,032	49,116	52,917	49,246
Beans (bags)	5,503	5,532	7,227	7,323
Corn (bu.)	7,576	7,198	7,636	8,472
Cotton (bales)	492	645	740	680
Flaxseed (bu.)	745	2,085	3,166	3,576
Grain sorghums (bu.)	4,308	3,651	5,584	7,264
Hay, tame (tons)	11,618	11,507	12,229	13,061
Hops (bales)	174	176	213	203
Oats (bu.)	26,968	34,577	27,714	30,626
Potatoes, all (bu.)	55,973	79,323	75,142	69,798
Early	5,411	11,089	10,260	10,333
Late	50,562	68,234	64,882	59,463
Rice (bu.)	8,176	9,000	8,968	10,212
Rye (bu.)	811	975	1,306	1,635
Sugar beets (tons)	2,897	4,375	4,448	3,435
Sweet potatoes (bu.)	1,204	1,200	1,440	1,560
Wheat, all (bu.)	105,916	98,620	100,908	128,496
Spring wheat	39,295	26,640	30,991	25,395
Winter wheat	66,621	71,980	69,918	103,101
Citrus Fruit Crops				
Grapefruit (boxes)	2,271	4,624	4,875	4,574
Lemons (boxes)	8,813	11,106	11,963	17,072
Oranges, all (boxes)	37,448	41,850	44,924	47,692
Navel	16,055	18,400	18,041	19,972
Valencia	21,393	23,450	26,883	27,720
Deciduous Fruit Crops				
Almonds (tons)	14	19	10	7
Apples (bu.)	43,949	39,893	39,720	40,872
Apricots (tons)	248	323	116	217
Cherries (tons)	61	88	69	72
Grapes (tons)	2,002	2,238	2,264	2,434
Wine	497	569	607	590
Table	362	373	448	423
Raisin	1,143	1,296	1,209	1,421
Peaches, all (bu.)	25,000	26,651	26,306	24,851
Clingstone	15,143	15,501	14,709	13,626
Freestone	9,857	11,150	11,597	11,225
Pears, all (bu.)	18,277	20,730	20,164	19,731
Bartlett	13,584	14,529	13,407	14,081
Other	4,693	6,201	6,757	5,650
Plums (tons)	65	71	69	71
Prunes, all (tons)	677	674	519	624
Fresh	69	91	67	86
Dried	232	213	178	199
Walnuts (tons)	46	59	46	58
Livestock and Related Products				
Chickens (head)	45,452	47,037	39,641	46,131
Eggs (dozen)	313,330	260,080	290,600	291,670
Hogs (head)	1,877	2,560	2,383	2,435
Lambs (head)	8,564	8,892	8,465	8,705
Turkeys (head)	4,102	6,470	6,632	6,880
Wool (lbs.)	101,121	99,093	97,049	98,745

Source: United States Department of Agriculture.

While exports have revived in the aggregate, the distribution of items making up recent shipments abroad has been markedly different from that prior to the out-

break of the present war. Shipments have been comprised chiefly of essential foodstuffs which are concentrated and of high nutritive value. The result has been that products previously not exported in large volume have accounted for a considerable part of the expansion in exports during recent months. These products include items such as condensed, evaporated, and dried milk, eggs, cheese, canned and pickled meats, rice, and cornstarch.

While agriculturists in the Twelfth District have shared in the recent improvement in exports of the commodities mentioned in the last paragraph, important foreign outlets for deciduous fruits (fresh, dried, and canned), and walnuts, which were lost earlier, have not been recovered. Purchase programs of the Federal Government and increased domestic demand, however, have provided an active market at prices substantially higher this season than last for these items. As shown in the accompanying tabulation, output of deciduous fruits and walnuts, of grains, and of citrus fruits in this area is larger than in 1940 and of near-record proportions. Only the production of almonds, sugar beets, hops, and barley is expected to be much smaller than the large crops of 1940. It is estimated that the district output of beans, cotton, flaxseed, grain sorghums, oats, rice, wheat, grapes, lemons, oranges, walnuts, butter, cheese, eggs, milk and milk products, and several vegetables for canning will be exceeded by output in only one or two previous years.

Banking and Credit

Loans of member banks in the seven larger district cities continued to expand during the four weeks ending October 22. As in recent months, this expansion reflected a further large increase in loans for commercial and industrial purposes which advanced an additional \$19,000,000 during the four week period to \$487,000,000, 39 percent higher than a year earlier. Other classes of loans fluctuated narrowly with little net change at about the levels of the mid-year. Reflecting allotments of bonds in the recent Treasury issue dated October 20, investments of these banks in United States Government obligations increased further.

The expansion in loans and investments of district city banks in recent weeks is a continuation of the persistent increases in both classes of earning assets reported by all district member banks as a group during the previous two years and more. As shown in the accompanying table, loans of all district member banks increased from \$1,872,000,000 on June 30, 1939 to \$2,386,000,000 on September 24, 1941, a gain of 27 percent. Investments in United States Government obliga-

UNITED STATES EXPORTS OF SELECTED AGRICULTURAL PRODUCTS—QUANTITY BASIS
(in thousands of tons)

Year ¹	Cotton ²	Fresh Fruits			Dried Fruits					Canned Fruits				Wheat	
		Apples	Oranges	Pears	Apples	Apricots	Prunes	Raisins	Total	Apricots	Salad	Peaches	Pears		Total
1928-29	8,739	505	148	41	25	12	137	111	303	13	16	51	41	164	3,093
1929-30	7,239	247	129	31	12	10	71	64	167	17	15	37	27	142	2,765
1930-31	7,180	488	139	67	19	12	148	63	258	10	16	38	37	136	2,291
1931-32	9,134	433	124	45	16	19	122	61	234	12	16	33	36	125	2,896
1932-33	8,865	330	119	60	18	17	91	56	199	10	13	38	30	119	627
1933-34	8,582	303	121	56	19	18	101	47	204	12	20	41	39	149	564
1934-35	5,328	193	143	50	12	8	76	47	157	5	16	25	36	118	90
1935-36	6,702	294	191	62	16	13	109	55	210	13	20	51	41	170	9
1936-37	6,062	162	108	66	11	15	82	56	179	12	19	30	33	136	95
1937-38	6,252	263	208	67	12	16	107	71	223	13	16	128	30	128	2,512
1938-39	3,874	290	265	85	16	14	107	77	236	17	22	48	39	175	2,538
1939-40	6,903	77	135	47	8	16	60	63	162	17	23	43	31	168	709
1940-41	1,283	21	146	12	1	1	19	43	70	(³)	2	2	1	8	324

¹Beginning July 1.

²Thousand bales.

³Less than 500 tons.

Source: United States Department of Agriculture.

tions were increased \$240,000,000 during the same period, a gain of 18 percent.

Approximately half the increase in total loans in the two-year period from June 30, 1939 to June 30, 1941 was accounted for by loans for commercial and industrial purposes which rose \$202,000,000. (A breakdown of loans of all district member banks by types is not available for the latest call report date, September 24, 1941.) This expansion in commercial and industrial loans partly represents the extension of bank credit to finance defense activity. On April 30, 1941 member banks in the seven larger district cities reported defense loans of \$34,100,000 outstanding and available information suggests that, as of that date, defense loans of all member banks in the district amounted to slightly less than \$40,000,000. By June 30, 1941 defense loans probably substantially exceeded this total, and consequently accounted directly for more than 20 percent of the total increase in commercial and industrial advances in the two years ending on that date.

EARNING ASSETS OF TWELFTH DISTRICT MEMBER BANKS
ON SELECTED CALL DATES

	(in millions)			
	June 30, 1939	June 29, 1940	June 30, 1941	Sept. 24, 1941
Total loans.....	\$1,872	\$1,978	\$2,279	\$2,386
United States Govt. securities....	1,354	1,405	1,553	1,594
Other securities.....	527	558	562	550
Total	\$3,753	\$3,941	\$4,394	\$4,530

An expansion of \$123,000,000 in loans on real estate, accounting for approximately 30 percent of the increase in total loans during the two-year period was traceable entirely to an expansion in advances secured by residential properties. Advances secured by farm lands declined \$8,000,000 and loans secured by other real estate (excluding residential properties) decreased \$18,000,000.

Expansion in loans in the miscellaneous "other" loan classification likewise increased considerably during the two-year period, rising \$90,000,000. Loans in this classification consist principally of personal and retail installment loans.

In contrast to the substantial expansion in member bank credit to finance commercial and industrial activity, the purchase of residential real estate, and consumer purchases, loans to finance securities transactions declined \$16,000,000. Loans for agricultural purposes (excluding advances on farm lands), and holdings of open market paper of district member banks were about unchanged from June 30, 1939 through June 30, 1941.

Gains in investments of district member banks principally reflected additions to holdings of United States Government securities. Investments in these securities increased \$199,000,000 from June 30, 1939 to June 30, 1941 and rose \$41,000,000 further by September 24.

Recent developments may have the effect of curbing, to some extent, further expansion in loans to finance transactions in residential real estate and to finance consumer purchases. The August and September declines in new residential building in the Twelfth District and the extension of priorities control to building materials have been discussed in another section of this issue of the Review. These developments may well result in some lessening in the demand for bank credit in this area to finance the construction and purchase of new housing

and it has been this demand that has occasioned much of the increase in loans of district member banks secured by residential properties over the past two years.

An Executive Order of the President, dated August 9, directed the Board of Governors of the Federal Reserve System to regulate the terms of consumer credit. Shortly thereafter the Board adopted Regulation W, most of the provisions of which became effective on September 1. Under this regulation, control is exercised over the extension of installment credit for financing or refinancing the purchase of consumers' durable goods. Principal provisions of the regulation cover the minimum size of required down payments and the maximum length of time over which installment loan contracts may be written. To the extent that this regulation, by increasing, in a number of cases, the required down payments and the size of the monthly installment payments serves to curb buying of durable consumers' goods, it will tend to check further expansion in miscellaneous "other" loans. Loans in this classification, it has already been noted, increased \$90,000,000 in the two years ending June 30, 1941. On that date, the aggregate of these loans reported by Twelfth District member banks amounted to \$440,000,000, of which \$329,000,000 consisted of personal and retail installment loans. This total of \$329,000,000 represented an increase of \$59,000,000 during the first half of 1941, a period during which total loans in the miscellaneous "other" loan classification increased only \$44,000,000.

It is consequently evident that in two of the broad directions in which credit expansion of district member banks has taken place since shortly before the outbreak of the present war, (the extension of loans to finance new private residential construction and consumer buying of durable goods) direct measures have recently been instituted which may check the rate of expansion in the immediate future.

Of a somewhat different character is the increase in reserve requirements announced by the Board of Governors of the Federal Reserve System on September 24, to become effective on November 1. The action taken by the Board was explained at the time of announcement as "a further step in the Government's program for combating inflation." Its effect in the Twelfth District will be to absorb some \$91,000,000 of excess reserves of local member banks. The existence of large excess reserves constitutes something of a potential threat of an excessive use of bank credit and the reduction in excess reserves tends to lessen that threat. As a credit control measure, an increase in reserve requirements has a broad or blanket application and contrasts, in this respect, with the more selective application inherent in measures such as Regulation W.

Even after the increase in reserve requirements on November 1, district member banks as a group will continue to hold a substantial amount of excess reserves, an amount ample or more than ample to meet all local credit needs of the defense program and all legitimate requirements of their customers. During the first half of October, total reserves of district member banks averaged \$916,300,000 of which \$325,000,000 consisted of excess reserves. Based on these figures, the banks will hold excess reserves of approximately \$234,000,000 after the November 1 increase in requirements.

Summary of National Business Conditions

Released October 20, 1941—Board of Governors of the Federal Reserve System

INDUSTRIAL activity continued at a high rate in September and the first half of October. Further advances in the output of defense products were accompanied by curtailment in some lines of civilian goods, particularly automobiles, rubber, and silk. Prices of industrial products increased but agricultural prices declined after mid-September, and on October 16 dropped sharply in response to international developments.

PRODUCTION

Industrial output increased by about the usual seasonal amount in September and the Board's adjusted index remained at 160 percent of the 1935-1939 average, the same as in July and August. Continued increases in activity were reported in the machinery, aircraft, and shipbuilding industries. At steel mills activity in September and the first half of October was maintained at about 97 percent of capacity. Output and deliveries of nonferrous metals likewise remained at about capacity levels, while lumber production declined somewhat from the high August rate. Automobile production increased less than seasonally in September, following the changeover to new models, and, according to preliminary estimates, output in September was considerably below the maximum quota that had been authorized by the Government.

In the textile industry activity declined somewhat in September, reflecting mainly a further sharp reduction at silk mills. Activity at wool mills rose to a new high level, while at cotton mills there was little change from a rate slightly below the peak reached last May. Shoe production continued in large volume, and output of manufactured food products was maintained near the peak August level. Output of chemicals likewise continued at earlier high rates, but at rubber plants activity was considerably below the level of last summer owing to curtailment programs ordered by the Government.

Coal production, which during the summer months had been unusually large, increased less than seasonally in September, owing in part to temporary work stoppages at some bituminous and anthracite mines. Crude petroleum production advanced to record levels in September and the first half of October, and output of metals and shipments of iron ore down the Lakes continued at about capacity.

Value of construction contract awards declined in September, according to figures of the F. W. Dodge Corporation, reflecting chiefly decreases in awards for public projects which had been exceptionally large in August. Awards for private residential building also declined, while contracts for other private work increased somewhat further. Total awards in September, as in August, were 80 percent larger than in the corresponding period last year. This higher level reflected mainly a greater amount of public construction, which was nearly three times as large as a year ago, compared with an increase of about 10 percent for private construction.

On October 9, the Supply Priorities and Allocations Board announced that, effective immediately, no public or private construction projects which use critical materials could be started during the emergency unless these projects were either necessary for direct national defense or essential to health and safety.

Distribution of general merchandise showed less than the customary seasonal rise in September, following an unusually large volume of sales in August. During the past three months sales have been larger than in the corresponding period of any previous year. In the first half of October sales at department stores declined from the peak reached in late September when there were considerable consumer purchases, particularly of articles subject to higher taxes on October 1.

Loadings of revenue freight in September increased less than seasonally, particularly those of miscellaneous freight, which have been high in recent months, and loadings of coal, which were curtailed during part of the month by work stoppages at some mines. Shipments of forest products declined from the high August level.

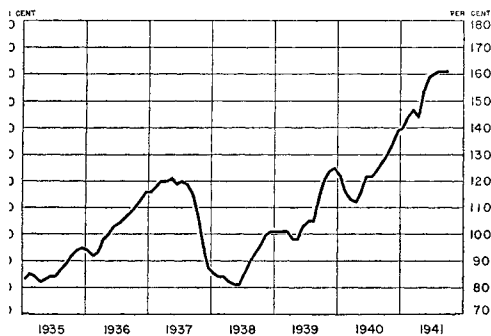
COMMODITY PRICES

Prices of industrial products continued to advance in September and the first half of October and Federal price ceilings were announced for additional commodities, including leading types of lumber, coke, wastepaper, paperboard, acetic acid, alcohols, and carded cotton yarns. In some cases these ceilings were below previously existing market quotations. Price advances were permitted, however, for some other commodities under Federal control. Prices of cotton and of foodstuffs increased further in the first half of September, but subsequently declined, owing partly to seasonal influences. On Thursday, October 16, prices of these commodities dropped sharply.

BANK CREDIT AND GOVERNMENT SECURITY MARKET

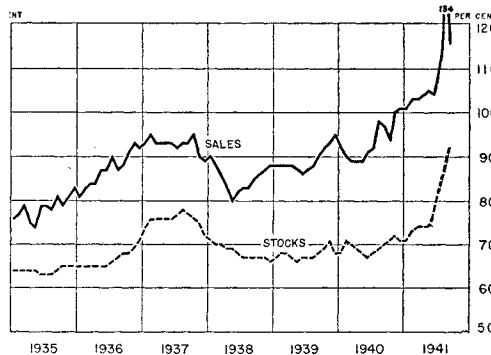
Commercial loans at member banks continued to rise during September and the first half of October, reflecting in part defense demands. Increases were substantial both in New York and in other leading cities. Holdings of United States Government obligations decreased, mainly at banks in leading cities outside of New York. Excess reserves of member banks showed little change in this period.

Following a slight decline in the first half of September, prices of long-term Treasury partially tax-exempt bonds increased during the latter half of September and in the first part of October. The yield on the 2¾ percent bonds of 1960-65 reached a new record low of 2.01 percent in October. Prices of taxable bonds moved within a relatively narrow range during the period with yields slightly above previous low levels.



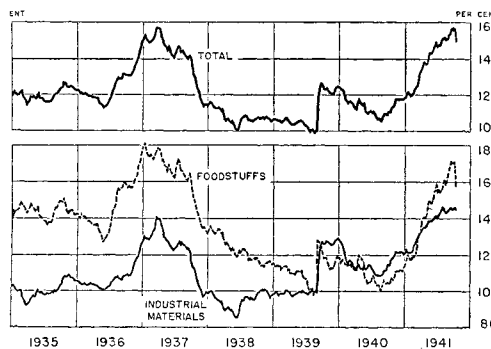
INDUSTRIAL PRODUCTION

Federal Reserve index of physical volume of production, adjusted for seasonal variation, 1935-39 average=100. By months, January 1935 to September 1941.



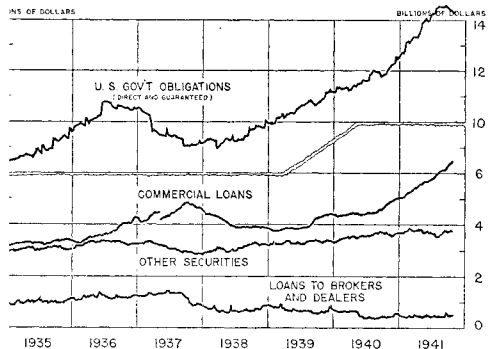
DEPARTMENT STORE SALES AND STOCKS

Federal Reserve indexes of value of sales and stocks, adjusted for seasonal variation, 1923-25 average=100. By months, January 1935 to September 1941.



WHOLESALE PRICES OF BASIC COMMODITIES

Bureau of Labor Statistics' indexes based on 12 foodstuffs and 16 industrial materials, August 1939=100. Thursday figures, January 3, 1935 to October 16, 1941.



MEMBER BANKS IN 101 LEADING CITIES

Wednesday figures, January 2, 1935 to October 8, 1941. Commercial loans, which include industrial and agricultural loans, represent prior to May 19, 1937, so-called "Other loans" as then reported.

Defense Savings Bonds and Payroll Deduction Plans

THE American economy is currently undergoing a major transition in the shift of productive capacity from peace-time to war-time industries. With idle productive capacity now practically eliminated, further expansion of defense output, apart from that resulting from continued additions to existing plant, is possible only through increasing interference with the production of consumer goods. Priority regulations and allocations are diverting more and more materials from ordinary to emergency uses, and conversion of plants to defense production is continuing apace.

The point cannot be overemphasized that, even with production expanded to the maximum, sufficient goods cannot be produced to satisfy *both* civilian and defense demands, and that in such a situation the civilian demand is obviously the one which must give way. The only real question, therefore, relates to *how* the necessary restriction in civilian consumption is to take place. Only three alternatives exist: (1) voluntary restriction; (2) restriction achieved by taxation and other forms of legislative compulsion; and (3) inflation, that more insidious form of "compulsory" restriction which limits consumption by the simple but arbitrary process of reducing the purchasing power of the consumer's dollar. Dollar incomes of consumers are rising, but this situation does not alter the physical fact that fewer automobiles, fewer stoves, and fewer refrigerators will be produced next year. If fewer goods are to be produced, it inevitably follows that fewer goods are to be consumed. Should consumers continue to spend all their increased income in the face of this restricted output, the result would be a rise in prices with no appreciable change in the physical volume of goods available for consumption.

There can be no doubt that the first alternative is the most acceptable in a free economy such as the United States, and, to the extent that voluntary restriction of consumption is embraced and practiced by the public, the necessity for legislative restriction is lessened and the threat of compulsory restriction by inflation is obviated. Not only is voluntary restriction on consumption in greater accord with our concept of individual liberty, but it also alleviates the problem of post-war adjustment.

A pattern of war-time saving which places a vast army of consumers in a position later to obtain spendable funds will enable them to purchase goods and thereby tend to sustain demand during that critical post-emergency period when defense requirements are drastically curtailed.

For these reasons, it is most desirable that the general public voluntarily restrict its consumption. The resulting savings can be practically and profitably invested in United States Defense Savings Bonds. While Defense Savings Stamps and Bonds may be obtained at post offices, most banks, building and loan associations, and other designated issuing agencies, and stamps may be obtained at many retail stores as well, the most convenient method of purchase for many people is through a Voluntary Payroll Deduction Plan. Under such a plan, an employee may authorize a specified deduction from his or her salary for the purpose of purchasing Defense Savings Bonds when accumulated deductions are adequate to effect such purchases.

Voluntary Payroll Deduction Plans have already been established by many industrial, financial, and governmental institutions. Their extension should be widely approved and encouraged. Through such programs the following desirable results are achieved:

1. Restriction of consumption, something which must occur in any event, is placed on a voluntary rather than a compulsory basis.
2. The diversion of consumer income from purchase of goods to purchase of bonds lessens the upward pressure on the price level, and thereby aids in keeping down both the cost of living and the cost of rearmament.
3. Savings invested in Defense Bonds aid the government in meeting the cost of defense.
4. Purchasing power withheld from civilian expenditure at this time, when industrial facilities are fully employed and unable to meet all demands, will be available for expenditure at some future date when curtailment of defense demands threatens to lead to decreased production and employment.