

Monthly Review

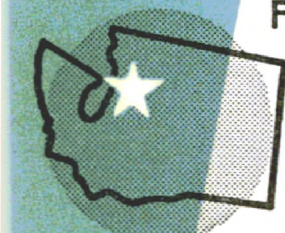


ALASKA

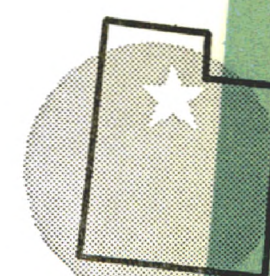


IDAHO

FEDERAL RESERVE BANK OF SAN FRANCISCO
TWELFTH FEDERAL RESERVE DISTRICT

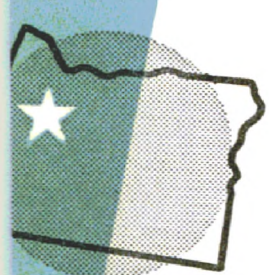


WASHINGTON



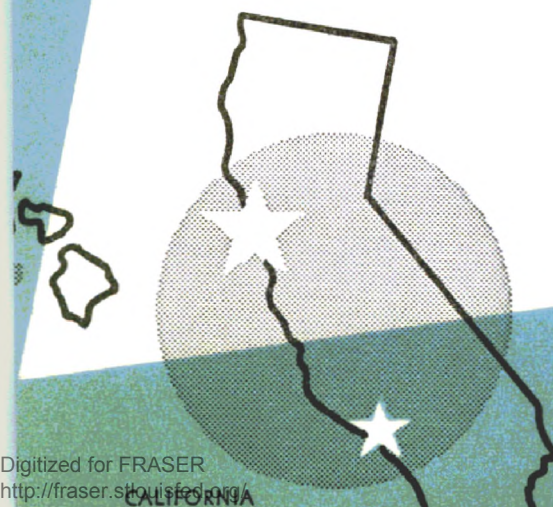
UTAH

Annual Review Issue

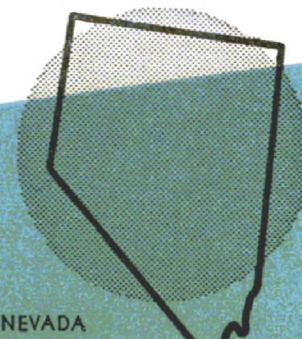


OREGON

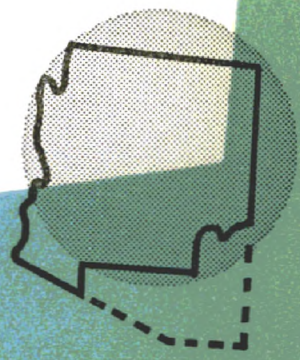
March 1962



CALIFORNIA



NEVADA



ARIZONA

1961: ANNUAL REVIEW



1961... ANNUAL REVIEW

CHINESE communities in the Twelfth District celebrated in late February the new year of 4660, the Year of the Tiger. The tiger is an interesting symbol standing for a variety of military virtues—such as dignity, sternness, courage, and fierceness; its parts may be employed for medicinal purposes (its whiskers, we are assured, will cure toothaches); and it scares away malignant spirits. Of more relevance, the tiger also stands for wealth, and the new year has been greeted as one which will see a strong business situation. The hesitation evident in the national statistics in January and, to some extent, in February have suggested to some observers that the year may turn out to be symbolized by a pussycat rather than a tiger.

In this, our annual review of the District, the data employed are naturally those of the past. It is important to know where you are before deciding where you are going. To help pinpoint the economic situation in the District, the course of our most recent recovery and expansion is compared with the two prior postwar business cycles in all cases where data permit. This should give some clues as to the character of the expansion currently under way.

The low point in national economic activity in the last recession occurred in February 1961, according to the National Bureau of Economic Research. The last 10 months of 1961 were characterized by recovery and expansion. In this article, the extent of recovery in the Twelfth District in the 10-month period from March through December 1961 is compared with that which occurred in the first 10 months of recovery in 1958-59 and 1954-55, again using the National Bureau's reference troughs for national activity as the basis for dating the start of recovery. Before examining District developments in detail, it will be helpful to review briefly the course of national business activity last year.

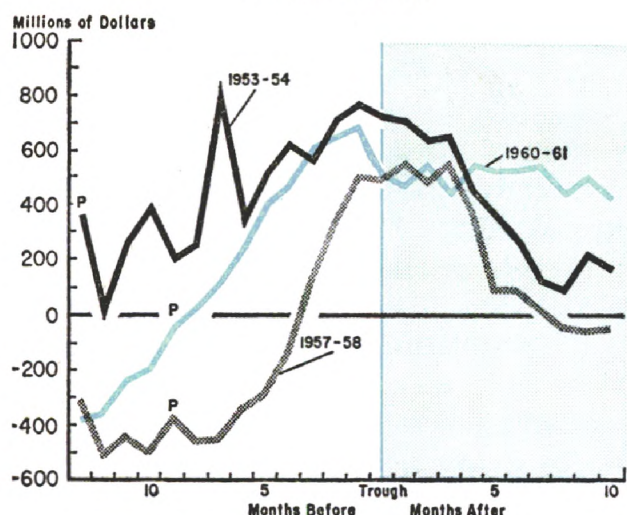
Nationally, a swift recovery from a mild recession

As 1961 began, the United States economy was still in the grip of a recession. Almost 7 percent of the labor force was unemployed and nearly one-fifth of manufacturing capacity idle. Although the business downturn was proving to be relatively mild and was generally expected to end by midyear (as it turned out, it was the mildest of four postwar recessions, and it ended in the first quarter), there was little expectation of a particularly boisterous recovery. Perhaps the optimists were still smarting from the high expectations which had been held for 1960 and were still awaiting fulfillment as that year ended. Whatever the reason, few observers were publicly prepared for the type of expansion pattern that emerged as 1961 unfolded.

Between the first and last quarters of 1961, gross national product rose from an annual rate of \$501 billion to \$542 billion. By mid-year industrial production had regained its previous peak level, and by December had risen 13 percent from its recession low. Reflecting these gains, nearly half of the plant capacity which was estimated as idle in January was in use in December; unemployment had fallen from 6.8 to 6.0 percent of the labor force; and the number of major labor market areas with a substantial labor surplus had declined from 101 in March to 60 in December.

Thus, the economy experienced in succession its mildest recession and its swiftest recovery in the postwar period. In outline, the developments from mid-1960 through mid-1961 were an example of the classic inventory cycle, in which reversals in inventory policy, particularly with respect to steel, were played out against a backdrop of relatively slight changes in final demand. If the cycle contained irregularities (and it is frequently difficult to say what is irregular and what is

CHART 1
NET RESERVES OF MEMBER BANKS
UNITED STATES



Source: Board of Governors of the Federal Reserve System.

not, since the business cycle itself is a conceptual generalization covering a host of irregularities), they were that the sharp expansion in business was not particularly reflected in unemployment rates or price indexes. If it had not been for the declines in November and December, the unemployment rate would have been as high at the end of the year as it had been in the preceding 10 months. Developments in prices were more encouraging. During the first three quarters of business expansion (through the end of 1961), virtually no signs of inflationary pressures were evident. Indeed, the record of price stability during 1961 was better than it had been in the recession.

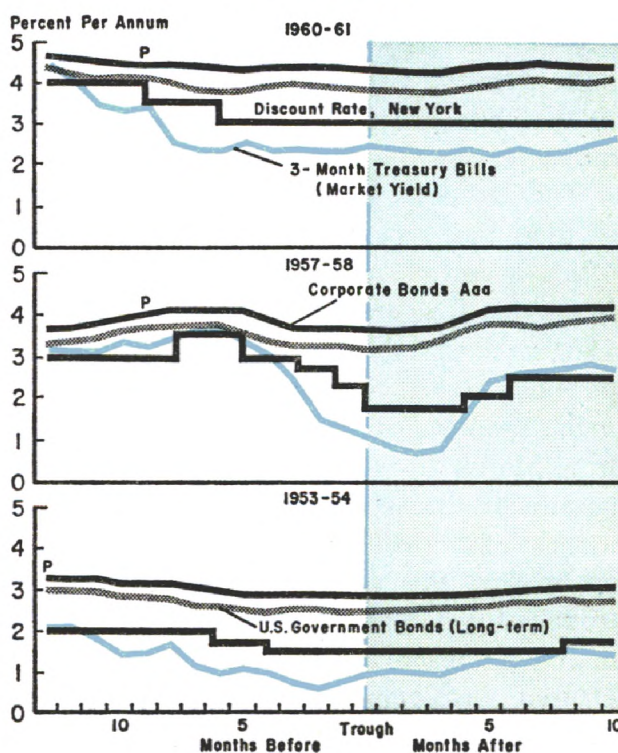
Monetary policy influenced by outflow of short-term funds

This type of economic atmosphere created no strong domestic wind against which monetary policy was required to lean in order to forestall inflationary developments. The formulation and execution of monetary policy were significantly influenced, however, by a factor that was absent in prior postwar recoveries, namely, a net incentive to invest United States short-term funds abroad and an incli-

nation and ability to take advantage of it. Following the introduction of nonresident convertibility of currencies throughout Western Europe at the end of 1958, a fully integrated and active foreign exchange market emerged which facilitated the international flow of short-term funds. The official concern over large outflows of short-term United States capital which had begun in mid-1960 in response to higher interest rates abroad led to a specific adaptation of monetary policy as one method of discouraging the outflow.

The discount rate, which had been reduced to 3 percent in August 1960, has since remained unchanged in order to help maintain short-term interest rates, particularly those on Treasury bills. The Treasury complemented this action by increasing the quantity of Treasury bills outstanding, thereby tending to depress their price and increase their market yield. In the second half of 1960, short-

CHART 2
SHORT- AND LONG-TERM INTEREST RATES
UNITED STATES



Source: Board of Governors of the Federal Reserve System.

term rates in the United Kingdom, for example, generally exceeded those in the United States by more than 1 percentage point after allowance for the cost of covering the exchange risk. Since mid-March 1961, however, the net incentive to hold United Kingdom Treasury bills has been much smaller and sometimes negative.

Federal Reserve open market operations were also adapted to help in maintaining short-term rates while at the same time supplying reserves as an aid to recovery and expansion. In two steps culminating in February 1961, the Federal Reserve System extended its operations in the open market to United States Government securities other than Treasury bills, this action being taken "in the light of conditions that have developed in the domestic economy and in the United States balance of payments with other countries." This new procedure permitted the System to supply needed reserves to the market by purchasing securities other than short-term Treasury bills. Moreover, at times long-term securities were purchased and short-term issues were sold simultaneously,

thereby helping to maintain or bolster the yields on short-term issues.

Changes in reserve requirements, the other principal tool of monetary policy, were not made during 1961. These were not needed since, within the range of limitation posed by the policy of maintaining or bolstering short-term rates, relative ease prevailed in the money and capital markets throughout 1961 without inflationary developments. Free reserves of member banks fluctuated around the \$500 million level during most of the year. This contrasted with the reduction of free reserves in the corresponding recovery periods of the two prior cycles.

For the reasons indicated, monetary policy contributed to the relative stability of interest rates during 1961, which contrasted with the larger amplitude of fluctuation in rates during the 1958 cycle. Although short-term rates rose a little as business expansion became more pronounced toward the end of the year, they did not rise much; long-term interest rates changed relatively little during the year despite a record volume of borrowing by State and local governments and corporations combined.

THE HOW AND WHEREFORE OF THE CHARTS

The charts that appear in this article are designed to compare the changes that have occurred in various economic indicators for the Twelfth District during the 1960-61 business cycle with those of prior postwar cycles. For this purpose, the dates for the peaks and troughs of the reference cycles for national economic activity, as determined by the National Bureau of Economic Research, have provided the framework on which the charts are drawn. In most cases, the data for Twelfth District economic indicators have been converted to an index with the trough month for each business cycle being calculated as equal to 100; in

a few cases, absolute amounts have been used instead. Since there were 10 months of recovery in 1961, data for only the first 10 months of recovery for prior business cycles are shown on the charts. The data have been carried back far enough from the troughs so that they include the peak of each cycle. These peaks are indicated by the letter "P" on each series.

It bears repeating that the peaks and troughs shown are not necessarily those for any of the individual indicators plotted but rather are those of the reference cycles for national business activity. The dates of those peaks and troughs are as follows:

Cycle	Peak	Trough
1953-54	July 1953	August 1954
1957-58	July 1957	April 1958
1960-61	May 1960	February 1961

RECOVERY IN TWELFTH DISTRICT BUSINESS ACTIVITY LESS RAPID THAN IN PRIOR CYCLES

Economic expansion following a recession has characteristically been more vigorous in the Twelfth District than in the nation, but during the first few months of recovery in 1961 the rate of economic expansion in the District lagged behind that of the nation. In the second half of the year, the District's rate of recovery compared more favorably with the national performance. The District's rate of expansion during the last 10 months of 1961 was significantly less, however, than in the corresponding periods of the two prior business cycles. This was most evident in the employment data, which provide the most comprehensive available measure of over-all economic activity for the District.

Growth in District nonfarm employment concentrated in second half of 1961

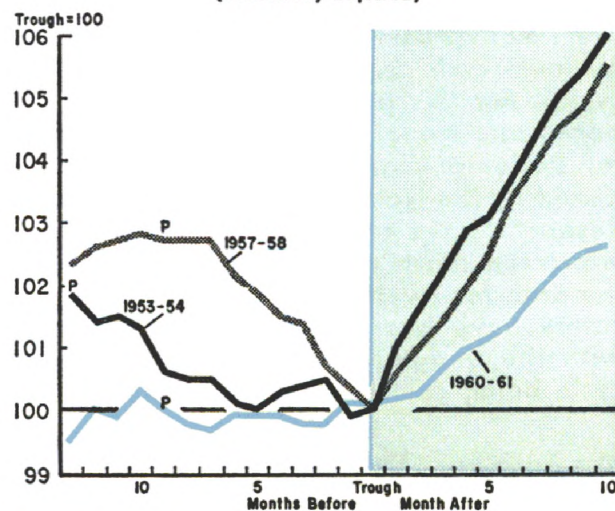
Although nonfarm employment in the Twelfth District (excluding Alaska and Hawaii)¹ reached a record high of 7,169,200 workers during 1961, the employment picture was dominated by the effects of the 1960-61 business cycle. Unlike the national experience, in which the peak occurred in May 1960, nonfarm employment in the District declined from March through July of that year (the rise in April was caused primarily by the addition of 19,400 temporary census workers). Following an increase in August, it changed little during the rest of 1960 and began to turn up in January 1961, two months earlier than in the nation. This pattern accounted for the increase of 8,600 workers in the District from May 1960 to

February 1961; however, this gain occurred only in the service-producing industries (trade, finance, and services) and in government. Employment in the commodity-producing industries (manufacturing, mining, and construction) and the related transportation and public utilities industry declined by 77,300 workers during the downturn, but this loss was only one-fourth as great as in the 1958 recession period, pointing up the mildness of this recession.

In the 10 months after the February turning point, nonfarm employment in the District expanded by over 2.5 percent. Gains of 3.2 percent occurred in the commodity-producing industries, 2.3 percent in the service-producing industries, and 3.4 percent in government employment, particularly in State and local units.

District manufacturing employment in the months of expansion grew rapidly after April, although less than one-half of the recession loss had been regained by July. By the end of 1961, the total loss of 55,900 workers that occurred between May 1960 and February

CHART 3
NONFARM EMPLOYMENT
TWELFTH DISTRICT
(Seasonally adjusted)



Source: State departments of employment.

¹Data for Alaska and Hawaii are not included in the totals mentioned in the text because seasonally adjusted figures, which are used frequently in the discussion, are not available for those two states. In 1961, nonfarm employment averaged 55,700 persons in Alaska and 187,200 in Hawaii, making a Twelfth District total of 7,412,100. Average employment in Alaska in 1961 was 2 percent below the 1960 level, largely because of a decline in contract construction activity, while Hawaii had a 2 percent increase with gains occurring in all industry divisions except manufacturing which had a small decline.

1961 had been recovered, and an additional 13,200 employees were at work. On an annual average basis, however, manufacturing employment in 1961 in the Pacific Coast States (where 92 percent of District manufacturing employment is located) was 1.2 percent (20,400 workers) below the 1960 level; losses were widespread despite sharp advances during the latter half of 1961.

In the durable goods sector, which has accounted for over 80 percent of the factory job loss in the past three downturns, all but one of the major industries suffered declines from the 1960 levels. The one exception was the electrical equipment and supplies industry in which the average number of jobs increased by more than 4.5 percent in 1961, reflecting the effects of increased defense expenditures. Employment in the transportation equipment industry, the largest hard-goods employer on

the Coast, fell by 4 percent. The gain of 15,500 jobs from June to December in the aircraft production centers did not offset the previous losses earlier in the year. Aircraft employment for the entire year, consequently, was down by 4.2 percent from 1960, continuing the sagging tendency in this type of activity that has been prevalent since 1959. West Coast shipbuilding and repair firms provided a bright spot within the transportation equipment industry; their average employment rose by almost 11 percent in 1961 and was at the highest level since 1953. However, this industry employs less than one-tenth as many workers as does the Pacific Coast aircraft industry. The industry with the largest relative decline was lumber and wood products, which had a job loss of over 14,000 in 1961 compared with 1960. This industry is discussed further on page 57.

TABLE 1
CHANGES IN TWELFTH DISTRICT EMPLOYMENT IN
THREE POSTWAR BUSINESS CYCLES

(Percentage changes from preceding peak to trough and from trough to 10 months after)

	Number employed ¹ December 1961	1960-61		1957-59		1953-55	
		Peak to trough	Trough to 10 months later	Peak to trough	Trough to 10 months later	Peak to trough	Trough to 10 months later
Nonagricultural	7,275.3	+0.1	+2.6	- 2.7	+ 5.5	-1.7	+ 6.0
Manufacturing	1,832.4	-3.2	+3.9	- 8.8	+ 8.3	-5.9*	+10.0
Durable goods ²	1,150.9	-4.5	+5.5	-12.0	+10.0	-8.4*	+14.4
Nondurable goods ²	547.8	-2.2	+2.2	- 2.9	+ 3.8	-1.9	+ 2.8
Mining	68.8	-3.0	+2.2	-11.5	- 1.1	-3.9	+ 4.9
Construction	427.3	-1.6	+0.6	- 2.4	+11.5	+0.2	+10.2
Commodity-producing ³	2,328.5	-2.9	+3.2	- 7.7	+ 8.5	-4.6	+ 9.8
Transportation and public utilities	523.3	-2.3	-0.1	- 6.0	- 0.5	-5.3	+ 3.7
Trade	1,589.6	0.0	+1.7	- 2.7	+ 4.6	-0.9	+ 4.1
Finance, insurance, and real estate	352.4	+2.7	+1.7	+ 2.6	+ 4.4	+2.7	+ 5.8
Services	1,089.3	+3.8	+3.4	+ 1.9	+ 6.4	+1.1	+ 5.3
Service-producing	3,031.3	+2.1	+2.3	- 0.6	+ 5.2	+0.1	+ 4.7
Government	1,392.2	+2.8	+3.4	+ 2.8	+ 3.5	+1.8	+ 3.3

¹ In thousands, seasonally adjusted.

² Pacific Coast States only.

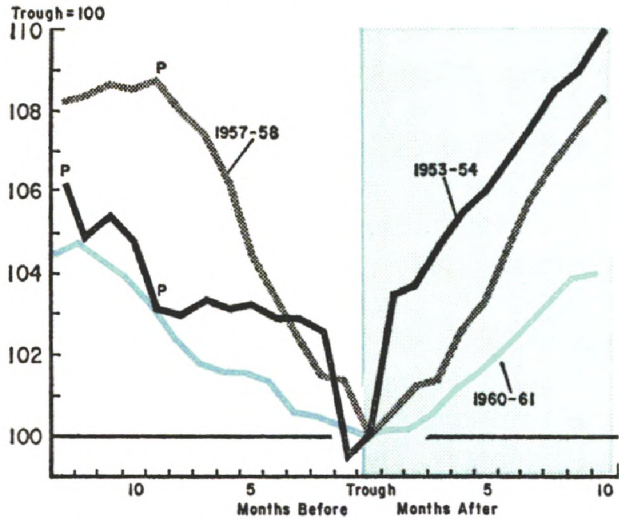
³ Manufacturing, mining, and construction.

⁴ Trade, finance, and services.

*Manufacturing employment was depressed in the 1954 trough by a strike in the lumber industry.

Source: State departments of employment.

CHART 4
MANUFACTURING EMPLOYMENT
TWELFTH DISTRICT
(Seasonally adjusted)



Note: Manufacturing employment was depressed in the 1954 trough by a strike in the lumber industry.
Source: State departments of employment.

Employment in nondurable goods industries for the year also declined, but this loss was only one-third as great as in durable goods. Jobs in food and kindred products fell by 1.4 percent, and in textiles and apparel, by almost 2 percent. These declines were partly offset by continued growth in the printing and publishing industries (up 2.8 percent over 1960) and a moderate rise in paper and allied products employment.

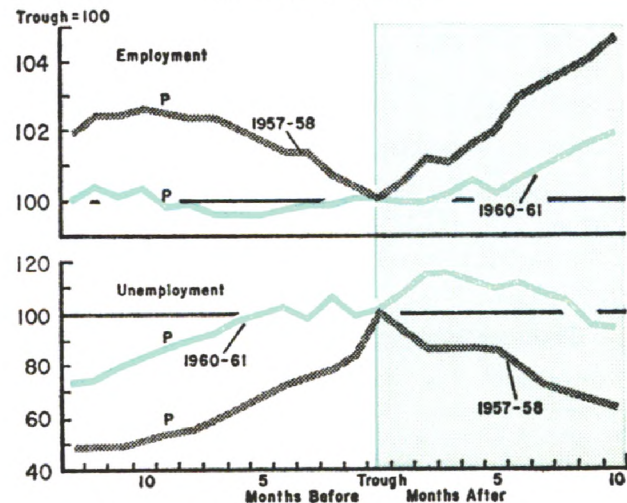
Although employment in mining rose by 2 percent between February and December, this industry had been in a slump since the 1958 recession, and the 1961 annual average employment was 0.7 percent below 1960. The level of employment in contract construction fell by 7,000 workers during the 1960 downturn, and by December 1961 only slightly more than one-third of the job loss had been regained. Employment in transportation not only failed to recover during the expansion but continued to decline.

In the service-producing industries, the finance, insurance, and real estate group and the services group in the District showed the same pattern of continued growth during the

1961 business cycle as in the two previous cycles. Employment in these two industry groups expanded by 47,800 employees from May 1960 to February 1961; 10 months after the trough, another 40,700 jobs had been added. Nevertheless, the rate of growth in these industries was not so great in this recovery period as in 1958 and 1954. Employment in wholesale and retail trade did not decline, as it did in the prior recessions; but by December the expansion in trade was far below the high levels reached in corresponding periods—1.6 percent by December compared with 4.6 percent by February 1959, and 4.1 percent by June 1955.

For 1961 as a whole, nonagricultural employment in the District averaged 95,300 more than in 1960, in contrast to the loss of almost 300,000 in the nation. The number of jobholders in government was 4.4 percent greater than in 1960; in services, 4.5 percent; and in finance, 2.8 percent. Trade employment was up by only 14,100 in 1961, one-quarter of the increase between 1959 and 1960. Manufacturing employment, which averaged 1,792,300 in 1961, was 15,500 below the previous year's level. Also, employment in contract construction was below the

CHART 5
CIVILIAN EMPLOYMENT AND UNEMPLOYMENT
PACIFIC COAST STATES
(Seasonally adjusted)



Source: State departments of employment.

1960 level by 5,200 employees, transportation by 10,000, and mining by 500.

The number of manufacturing production workers in the District fell below the 1960 average by 2.5 percent for the year. However, average hourly earnings were higher in 1961 and the workweek slightly longer; consequently, production workers took home an average weekly paycheck of \$106.79, up \$4.09 from 1960.

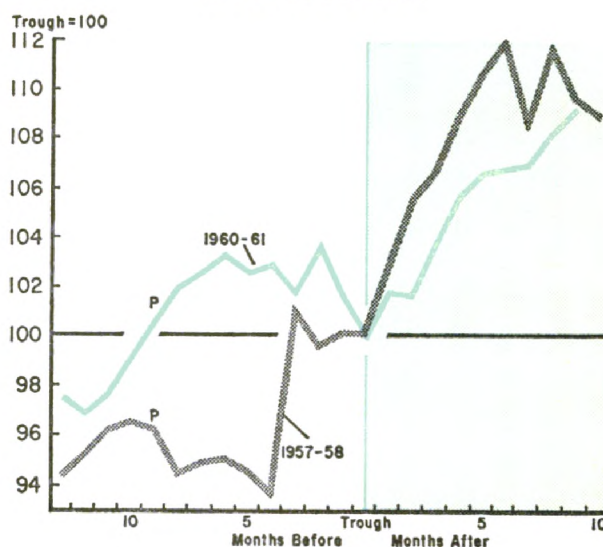
Personal income rose more rapidly than retail sales during 1961

Spurred by the recovery phase of the business cycle, total personal income and retail sales in the Twelfth District, as in the nation, reached record highs during 1961. Following much the same pattern as occurred in the 1958-59 recovery period, personal income grew at a faster rate than retail trade, possibly indicating some uneasiness on the part of consumers concerning future developments in view of the continued high unemployment rate.

The course of personal income during the post World War II period has been one of steady growth with but few moderate interruptions. The pattern of growth in the 1960-61 cycle was no exception. In the District and the nation, personal income continued to rise, albeit moderately, for five months after the May 1960 reference peak before declining gradually to the trough month of February. Coincident with the national economic upturn, income rose through the end of the year, with only one month's interruption. Reflecting larger relative gains in population and employment in the District than in the nation, personal income in the District had reached a level 10 percent above the trough month by the end of the year, while nationally it had risen only 6 percent.

Comparisons over the course of earlier business cycles are not available for District personal income except for 1957-59. The recovery pattern of the 1960-61 period was

CHART 6
PERSONAL INCOME
TWELFTH DISTRICT



Source: *Business Week*.

roughly similar to that of 1958-59, with personal income rising to about the same level above the trough at the end of 10 months. In the recovery phases of both of these cycles, it appears consumers were not willing to increase their purchases at as fast a rate as their incomes were growing. The dollar volume of sales by Group I retail stores¹ in the Twelfth District during 1961 was somewhat more than 1 percent above the 1960 level, while personal income rose about 5 percent. Similarly, sales had remained virtually unchanged during the 1957-58 cycle, while incomes rose.

District retail sales, on a seasonally unadjusted basis, generally conformed to the cyclical developments of 1960-61. Beginning in May of 1960, there was a virtually uninterrupted period of monthly declines from year-ago levels, although there was substantial variation in their intensity. After April 1961, sales showed a consistent rise in the magnitude of increase over the year-ago month. Although by November total cumulative sales for the year were slightly above those for the

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

comparable period in 1960, it was not until the December figures were available that the record sales year became a certainty.

This general pattern of behavior was shared to a large extent by all categories of stores. Sales of all types of soft goods stores showed considerable improvement during the recovery phase in 1961, with the exception of food lines. In the 1957-59 cycle, on the other hand, food sales increased continuously over the recession and recovery phases, reflecting, in part, a rise in food prices which did not occur to the same degree in 1960-61. Among the durable goods stores, household goods and building supplies never recovered in 1961 their year-ago levels, no doubt reflecting the lack of buoyancy in housing demand. However, sales of the automotive group (which accounts for more than 75 percent of all hard line sales) recovered sufficiently to bring total hard goods store sales to a level 1 percent above the total for 1960. Consumers apparently were cautious about committing themselves to longer term debts during the uncertainty of the early months of recovery; consequently, this had a restraining effect on sales of durable goods stores.

New car automobile registrations (unadjusted) may indicate more clearly the developments in the hard goods area. Registrations in the District turned up one month before the February 1961 trough and continued to rise for four months thereafter. The effects of lowered inventories and preparation for model changeovers resulted in a three-month downturn in the late summer. Auto sales did rebound sharply in October when the new models were unveiled, and more moderate increases occurred in November and December. National experience was quite similar to that of the District, though the magnitude of fluctuations from the trough month were much greater. District auto sales in 1961 were comparable with those in the 1958 recovery period, after correction for seasonal factors.

However, in the 1954-55 recovery, automobile registrations reacted spectacularly to the increased availability of credit and the easing of terms which occurred in the early part of 1955.

Consumer credit typically lags at start of an upturn

In the early months of the 1961 recovery, consumers throughout the nation were repaying their outstanding credit at a faster rate than they were borrowing. It was not until April that consumer debt began to rise. This reflected the softness in retail sales and the desire of consumers to become more liquid as evidenced by increased savings. However, as sales, especially of Christmas items and of automobiles, increased, consumer credit outstanding rose gradually. This type of pattern generally prevailed at all types of consumer lenders with the exception of banks. Loans outstanding at sales finance companies, however, dropped more in the earlier months than at other lenders, and it was not until the end of the year that loans regained their February level. As a result, the volume of bank borrowing by sales finance companies was relatively small.

In the nation and Twelfth District¹, the experience of commercial banks was markedly different from that of other consumer lenders. This was primarily the result of the purchase in early 1961 by quite a few banks of a substantial amount of consumer paper from a national retailer. As these loans were paid off monthly, they were not regenerated at banks; consequently, District banks holdings of "other consumer goods paper" declined gradually all year. Other types of bank consumer loans increased, although automotive credit outstanding rose less than in the other recovery periods. As a result of these movements, outstanding consumer credit held

¹The only consumer credit data regularly available for the District are those for commercial banks.

by banks in both the District and the nation began to decline in February and continued to drop in nearly every month of the 10-month recovery period of 1961. This is in sharp contrast with both 1954 and 1958. During 1954-55, a sharp rise in bank outstandings was accounted for largely by automobile financing, although personal loans also rose; while during 1958-59, there were moderate increases in automobile, other consumer paper, and repair and modernization loans.

District construction up in 1961

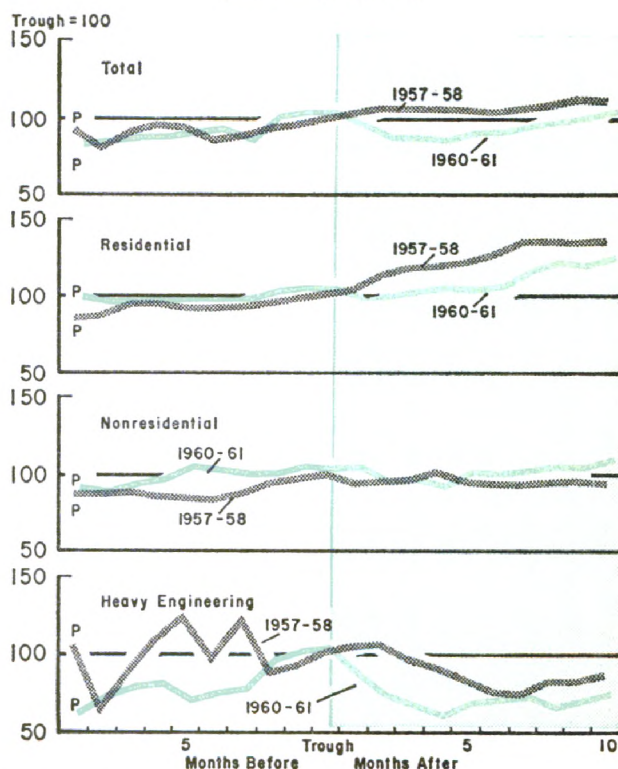
District construction, as measured by contracts let, recovered in 1961 from its slump in the preceding year. The dollar volume of all construction contracts awarded was slightly over \$7.5 billion, about 9 percent greater than the total for 1960. This was a more vigorous recovery than materialized nationally, where contracts rose only 2 percent above 1960. Nevertheless, the performance of construction in the recent economic recovery in the District was less impressive compared with earlier periods of recovery. The dollar volume of construction contracts began to pick up in the last half of 1960 while the District economy was still declining and continued to increase through the first two months of 1961. This increase was dominated by a sharp rise in contracts awarded for heavy engineering projects, particularly for new highway construction. Heavy engineering contracts began to level off in early spring, however, and were at relatively low levels throughout the rest of the year. The slow up in this type of activity was sufficient to push down the over-all level of construction until late in the summer when increasing levels of homebuilding along with a moderate rise in nonresidential construction helped push the total up again.

As a result of this pattern of events, construction made little positive contribution of its own to recovery in the District economy, despite the over-all increase in contracts

which occurred in the annual data. Contract construction employment in the District, for example, showed very little improvement from the time when the national economy started to turn up in March 1961. This was in marked contrast with the corresponding phases of the 1958-59 and 1954-55 recoveries when employment increased 12 and 10 percent, respectively. In addition, the dollar volume of construction contracts let, though it increased in the latter part of the year, was by the year end little improved from the level prevailing in February. In the 1958-59 recovery, on the other hand, there was steady improvement in contract awards over a corresponding 10-month period.

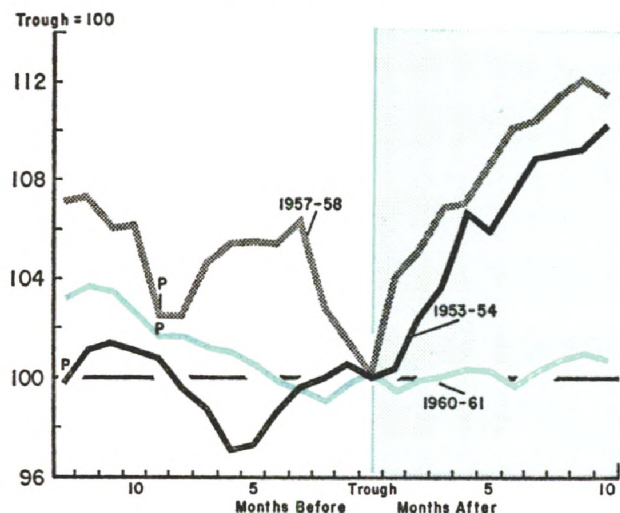
District residential construction, which sputtered along initially, began to pick up in late summer and accounted for most of the increase in total construction which took

CHART 7
CONSTRUCTION CONTRACTS AWARDED
TWELFTH DISTRICT
(Seasonally adjusted)



Note: Data plotted are three-month moving averages.
Source: F. W. Dodge Corporation.

CHART 8
CONTRACT CONSTRUCTION EMPLOYMENT
TWELFTH DISTRICT
(Seasonally adjusted)



Source: State departments of employment.

place in the latter part of the year. The construction of new residences held up as well as it did in the early part of 1961 because of a high level of multiple dwelling unit construction, which for the entire year was about one-third greater than in 1960. In the latter part of the year, however, single-family home construction began to rise. Coupled with the continued relatively high level of apartment building, this increase in home construction brought about a sustained rise in District residential construction.

The increase in home construction may have been due in part to "pent up" demand, that is, families who had held off coming into the market in 1960 may have decided that 1961 was the year to do something about their housing. Their actions had an impact on new construction because the "overhang" of unsold new housing had been pared down in some areas of the District, for example, Seattle, Portland, and San Diego. It may have also been, in part, a belated response to the relatively easy mortgage market conditions which prevailed throughout most of the year.

There were a number of indications which pointed to the availability of an adequate sup-

ply of mortgage funds. District savings and loan shares, for example, rose over \$2.5 billion, about one-fourth more than the increase in 1960. In addition, time deposits of commercial banks in the District rose \$1.7 billion or roughly three times the amount they increased in the previous year. Finally, the substantial increase in mutual savings bank deposits and in assets of life insurance companies nationally suggested that "Eastern" investors had an abundant supply of funds to invest in "Western" mortgages.

Interest rates were also lower, which in itself suggests increased availability of funds. The maximum rate on FHA-insured mortgages was, of course, cut twice during the year. The market response to the first of these (the cut to 5½ percent in February) indicated considerable ease in that the price discounts on FHA's declined despite the lower rate. The reduction to 5¼ percent in May resulted in somewhat larger discounts, but the increase was not sufficient to offset the lower rate, so that yields on these Federally insured mortgages declined further. Rates on conventional mortgages also declined somewhat. The Federal Housing Administration quarterly survey of the opinions of the Directors of its insuring offices, for example, indicated that by the end of the year the average interest rate on conventional first mortgage loans on new homes in the West declined to 6.20 percent from the 6.55 percent average that prevailed at the beginning of the year.

The role played by residential construction in the current expansion, though it has been a positive one, has been less impressive than its contribution in the earlier stages of prior postwar recoveries. Residential contracts rose by roughly one-fifth in the 10-month period following February, but this was less than their increase of more than one-third during a comparable period in the 1958-59 recovery. Contract data are not available before 1956, but the housing starts data for the

Western Region¹ suggest that the increase was substantially more in the 1954-55 recovery as well. This undoubtedly reflected, in part at least, some persisting weakness in demand. Vacancy rates, though they declined somewhat in a number of areas in the District, were still well above earlier levels. Another factor may have been the cost of mortgage funds, for although rates did decline throughout most of the year, they were also above earlier levels.

Nonresidential construction, which increased moderately in 1961, contributed to the recovery in the District's economy. This was in contrast with its performance in the early stages of the 1958-59 recovery when this type of activity declined. Nonresidential construction contracts made during the year amounted to \$2.1 billion, 6 percent higher than in 1960. This increase was due largely to rising levels of contracts for the construction of commercial, educational and science, and public buildings. Contracts for industrial buildings, which lagged behind 1960 levels during the first half of the year, picked up in the latter months, with the result that the total for the year was slightly above 1960.

Heavy engineering construction also increased in 1961. As already indicated, contracts for this type of construction, particularly for new highways, were at exceptionally high levels in the early part of the year but then declined. However, the volume of awards at the beginning of the year was sufficiently large so that the total of \$1.8 billion was 10 percent above 1960. The yearly increase was due mainly to a larger volume of contracts for utilities construction and, to a lesser degree, to increased contracts for streets and highway construction.

Lumber output declined in 1961

The lumber industry, which suffered a slump in 1960, showed very little recovery in

1961. Despite a small rise in homebuilding this past year, lumber output over the same period failed to reach its 1960 level, due perhaps to efforts on the part of mills to keep output more closely in line with new business, which was affected by the continued substitution of other materials for lumber in homebuilding and other types of construction.

Lumber output and employment in the District, which turned down in the early part of 1960, continued to decline in the early part of 1961. In early spring, however, mill orders for lumber increased abruptly, possibly as a result of dealer inventory accumulation in expectation of improvement in the level of homebuilding. This led to a sharp rise in lumber prices, which rose more than \$5 from the beginning of March to mid-April, and was followed by lumber output increases in April and May. Lumber employment also began to pick up about that time. New business, however, failed to maintain its early spring pace, undoubtedly due to the fact that the expected increase in housing starts never fully materialized. As a result, lumber prices began to fall in early summer, followed by a leveling off of lumber output and employment. Throughout the remainder of the year, production was kept pretty much in line with new business, which remained below the high levels attained in the spring of the year. This restraint on production kept inventories from increasing, which in the case of Western pine items was in sharp contrast with what happened in 1960. At the end of the year, Western pine inventories were 3 percent below the amount at the end of 1960, whereas Douglas fir stocks were 5 percent above.

Douglas fir lumber production for the entire year amounted to 7.8 billion board feet and was 7 percent below 1960. Western pine output was also below its 1960 level (3 percent). This was in contrast to the upward movements of both in the early stages of other

¹Includes Colorado, Montana, New Mexico, and Wyoming in addition to District States.

postwar recoveries in the District. Employment in the lumber industry, after declining in the first three months of the year, rose moderately over the next several months and then remained stable for the rest of the year. At the end of the year lumber employment in the District was about 6 percent above the February level, the low point for over-all economic activity in the nation. This, however, was substantially less improvement than occurred in the corresponding phases of the 1958 and 1954 recoveries.

Plywood production up moderately; prices soft

Plywood production in the District continued to expand in 1961, although, as in 1960, the increase was of modest proportions. Softwood plywood output amounted to 8.4 billion square feet, while 500 million square feet of hardwood plywood was produced. The combined total of nearly 9 billion square feet was 7 percent above total plywood output in 1960, marking the 16th consecutive year of growth in production.

Although total output rose, production was estimated to have averaged only about 75 percent of capacity during the year. The restraining factor, of course, was the disappointing level of sales. Increased production in the face of weak market conditions resulted in an average of plywood prices for the year that was at the lowest level on record. The price of quarter-inch sanded stock, for example, was at an all time low of \$60 per thousand square feet at the beginning of the year. In the spring, this price rose to \$72, but when housing demand failed to pick up as much as expected, it began to decline and continued to do so until it reached \$60 again in October where it remained for the balance of the year. The low prices during the year led the industry to conclude that 1961 was a year of "profitless prosperity."

Defense build-up aids in District expansion

Increased Federal government spending for national defense measurably added to the Twelfth District's income and employment during 1961. Slightly more than 30 percent of the \$22 billion value of prime contracts awarded for military procurement during fiscal 1961 went to District States. With defense expenditures still rising, the further growth of the defense industry in the District seems assured.

District employment in defense-related industries in 1961 approximated 600,000, or about one-third of manufacturing employment and about 8 percent of nonfarm workers in the District. The role of the whole complex of District defense and defense-oriented industry during fluctuations in the general level of business activity is difficult to analyze with precision. Much of the "defense industry" overlaps other industries. Electrical manufacturing for defense purposes is an integral part of electrical manufacturing in general. Missiles and components are produced by the same firms that produce civilian airplanes. Strictly naval defense work is only a part of total shipbuilding along the Pacific Coast. Chemical propellants are often made at the same places that fertilizers and industrial chemicals are produced. Sorting out the precise dividing line between defense and nondefense employment is therefore, at best, a difficult task.

There is, however, another peculiarity in the role of defense spending within the District. Defense spending should theoretically be largely independent of the business cycle. Yet, as Table 2 shows, virtually all of the defense-oriented industries within the District showed cyclical fluctuations. General recessions were accompanied by declines (or slower rates of increase) in employment; upswings, by rises.

TABLE 2
CHANGES IN TWELFTH DISTRICT DEFENSE EMPLOYMENT
IN THREE POSTWAR BUSINESS CYCLES

(Percentage changes from preceding peak to trough
and from trough to 10 months after)

Industry	1960-61		1957-59		1953-55		Average 3 cycles	
	Peak to trough	Trough to 10 months later	Peak to trough	Trough to 10 months later	Peak to trough	Trough to 10 months later	Peak to trough	Trough to 10 months later
Electrical machinery ¹	2.3	5.5	4.4	18.9	— 6.6	17.0	—2.9	13.8
Aircraft ¹	— 3.7	3.9	—14.8	4.8	6.5	3.3	—4.0	4.0
Private shipyards ¹	— 4.6	16.8	0.6	3.8	—15.7	18.7	—6.6	13.1
Ordnance ²	10.1	11.8	5.0	37.3	—14.2	38.7	0.3	29.3
Total	0.3	6.0	— 9.4	11.1	1.5	8.6	—2.5	8.6

¹ California, Oregon, and Washington.

² Arizona, California, and Utah.

Source: State departments of employment.

TABLE 3
TWELFTH DISTRICT EMPLOYMENT IN DEFENSE INDUSTRIES
IN THREE RECOVERIES

(Employment in thousands)

Industry and area	At trough February 1961	10 months later	At trough April 1958	10 months later	At trough August 1954	10 months later
Pacific Coast						
Electrical machinery	179.7	189.6	117.7	140.0	65.2	76.3
Aircraft	256.6	266.5	305.2	319.7	262.2	270.9
Private shipyards	16.7	19.5	15.8	16.4	15.0	17.8
Arizona						
Ordnance and aircraft	9.5	9.2	11.3	11.6	6.3	9.4
Machinery (including electrical)	9.9	10.3	5.2	6.1	1.6	2.3
California						
Ordnance	67.0	73.7	32.3	46.5	13.0	17.3
Instruments	22.3	23.6	20.3	21.6	13.5	15.0
Utah						
Ordnance and trans- portation equipment	10.6	14.5	2.2	4.8	0.1	0.2
Total	572.3	606.9	510.0	566.7	376.9	409.2

Note: Data are not adjusted for seasonal variation.
Source: State departments of employment.

Regardless of the possible existence of cyclical patterns in defense-oriented employment within the District, the growth of these industries has been impressive during the period under review. In each successive trough in general business, total employment in District defense-oriented industries has been at higher levels, as Table 3 shows. However, as indicated in Table 2, the percentage increase in this type of employment was smaller during the recovery period in 1961 than in comparable periods of the two preceding recoveries.

Within individual industries, there have been important shifts in demand. For example, the shift from aircraft to missiles put aircraft employment into a four-year slump from which it is only now beginning to recover. Such shifts alter the proportion of production workers to the dollar value of sales and can thus cause severe local effects, even when total dollar sales are rising.

Some observations stand out from the experience of the three recessions of the 1950's. First, only in the 1957 recession did total defense-related employment actually fall, and this decline was partly explained by the change from airplanes to missiles. Second, growth factors in these industries have outweighed the cyclical response pattern and probably will continue to do so while total defense expenditures are increasing. Third, there has been a cyclical pattern of sorts, but analysis of the causes of this pattern must await the development of better data.

Steel production fluctuated less in District than in nation

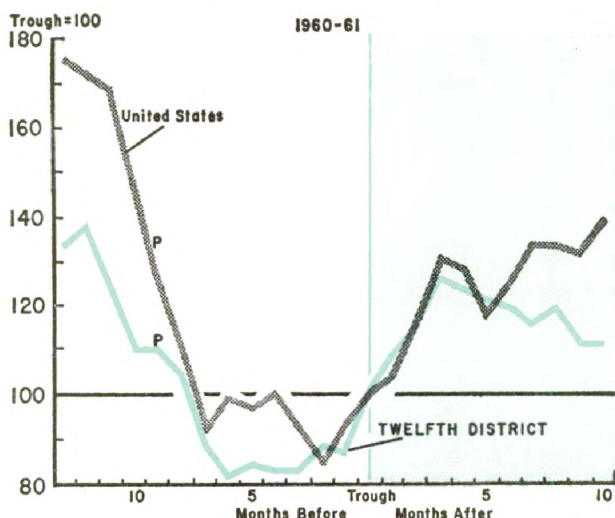
Twelfth District steel production, which turned up six months before general business, already had risen almost 26 percent from its own low point in August 1960 to the trough in business in February 1961. Because steel output in this District is less dependent on automobile production, its behavior was in contrast to national steel output which had

risen only 18 percent from its lowest level in December 1960 to February (Chart 9).

From February to May both District and national steel production advanced steadily, and by the end of that period the national index, responding to increased demand for steel by automobile assemblers, had moved ahead of the District index. Steel production then entered its usual summer slowdown. The national index started recovering in August, and by September, despite a strike at a major automobile company, it had exceeded the previous 1961 high for steel reached in May. With labor disputes continuing to affect the automobile industry, steel production in October was little changed from September; it fell in November, however, when automobile makers did not increase their steel purchases as they had been expected to do after the end of the auto strike. National steel production surged ahead in December under the impact of improved demand from the automobile industry and the beginning of stockpiling against the possibility of a steel strike in mid-1962. By December, a very favorable month for steel production, the national steel index had moved forward 39 percent from the February trough, while District steel output had risen only 10 percent. Nevertheless, even with its relatively milder decline in the recent recession, District steel production of 5.6 million tons for the year 1961 was nearly 11 percent above its 1960 level, whereas the 1961 total for the country as a whole was 1.3 percent shy of reaching its 1960 figure. The same pattern occurred in the recession and recovery periods of the two immediately preceding postwar cycles, when steel production in the District exhibited the greater stability, falling relatively less in recession and rising relatively more in recovery than steel in the nation.

The 10 percent advance in Twelfth District steel production during the 10 months after the business low in February 1961 was

CHART 9
STEEL PRODUCTION
TWELFTH DISTRICT AND UNITED STATES

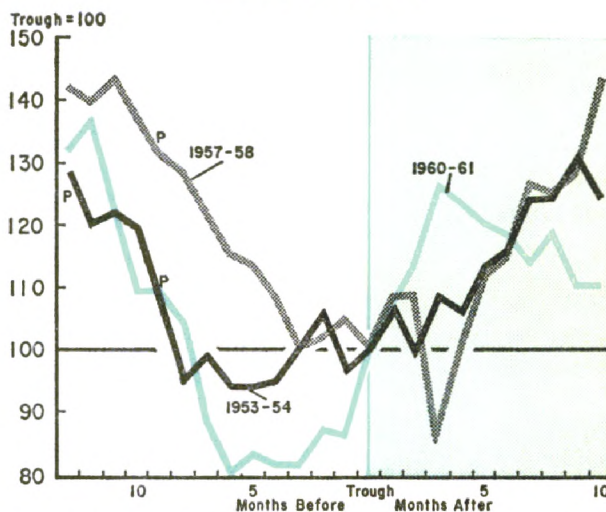


Source: American Iron and Steel Institute.

considerably weaker than the 24 and 43 percent increases registered in the comparable 1954-55 and 1958-59 expansion periods, respectively. The gain in national steel production 10 months forward from the bottom of the 1960-61 recession also was considerably less buoyant than the 51 and 86 percent rises of the two previous 10-month postwar recovery periods. The apparent mildness of the 1961 District steel expansion measured in this way is partly dispelled if it is recalled that production had already advanced substantially before February. Measured from the time it reached its lowest recession point in August 1960 to its December 1961 level, the 1961 advance outpaced the comparable 1954 rise by 6 percent. That it was only about 55 percent as high as in the 1958-59 period is understandable in that steel output in the later stage of that period was responding to the anticipation of the strike which came in July 1959.

The Western steel industry entered 1962 with high expectations which began to be realized in January when a marked upturn in Western steel orders and output occurred. Inventory building and strong demand from

CHART 10
STEEL PRODUCTION
TWELFTH DISTRICT



Source: American Iron and Steel Institute.

the West Coast construction industry, especially for missile base construction, are big factors in the optimistic forecast for the first half of 1962. Although imports of steel into Western states and the nation as a whole declined approximately 5 and 6 percent, respectively, these imports continue to equal about 13 percent of West Coast steel production and still offer considerable competition on selected items to Far Western steel producers.

Noncyclical factors affect copper production

Copper developments in 1961 were influenced as much by strikes and foreign activities as by cyclical factors. The first significant event for the copper industry in 1961 occurred in mid-January when major mine producers reduced prices by 1 cent for refined copper in an attempt to reduce the gap between domestic and foreign prices. Even with this reduction to 29 cents a pound, designed to stimulate demand, curtailments in output were put into effect in February, and District copper production from mines fell 4 percent in that month. In May, increasing domestic demand, higher prices in the world markets, political turmoil in the Congo, heavy United

FEDERAL RESERVE BANK OF SAN FRANCISCO

INDEXES OF INDUSTRIAL PRODUCTION—TWELFTH DISTRICT

(1947-1949 = 100)

INDUSTRIAL PRODUCTION	1946	1956	1957	1958	1959	1960 ^r	1961 ^p
Copper	71	131	130	116	99	129	136
Lead	70	80	79	62	63	52	66
Zinc	83	72	75	64	66	59	67
Silver	64	106	110	105	97 ^r	94	110
Gold	71	79	77	70	55 ^r	61	56
Steel Ingots	60	163	172	142	138	154	171
Aluminum	51	197	185	143	166	166	160
Crude Petroleum	94	105	101	94	92	91	92
Refined Petroleum	91	129	132	124	130	134	140
Natural Gas	89	92	90	86	93	100	103
Cement	81	156	149	158	174	161	169
Lumber	79	120	106	107	116	107	101
Wood Pulp	82	192	189	186	196	199	202
Douglas Fir Plywood	78	291	303	352	428	411	428
Canned Fruit	128	142	129	121	149	148	155
Canned Vegetables	124	225	194	214	190	202	207
Meat	101	149	139	127	134	143	145
Sugar	90	120	128	116	137	133	135
Flour	108	105	106	112	112	113	109
Creamery Butter	69	87	99	93	99	108	117
American Cheese	97	85	89	86	91	99	99
Ice Cream	132	114	120	126	129	127	132

p—preliminary r—revised

Note: Data given above supersede all previously published annual indexes.

Source: Federal Reserve Bank of San Francisco.

States exports of scrap copper, and the possibility of labor trouble about midyear when the contract at a major Western copper firm was due to expire were factors in an increase of 2 cents in the price of refined copper during the month and a 7 percent rise in Western copper production. More copper was used in products shipped during May from wire mills, brass mills and foundries than for any month since April 1945. New orders booked in May called for the use of more copper than in any month during the two previous years, and stocks of the metal at the mills and foundries were the smallest since February 1960.

Demand for copper subsided with the start of July and August vacation closings at consumer plants and the reduction of inventory hedge buying with the postponement of the

strike threat by production workers. A strike by a comparatively small number of specialized workers also contributed to a fall in output in August. Resuming its rise by September, District copper output had advanced 9 percent in the upswing from February through December. Increases 10 months from the respective troughs in 1954 and 1958 were 73 and 15 percent.

District copper production from mines in 1961 was 5 percent above 1960, but the share of national production accounted for by the District fell slightly from 78 percent in 1960 to 76 percent in 1961.

Contrary to their previous pattern in business recoveries, production of lead and zinc in the Twelfth District each declined 16 percent from February to December 1961. Nev-

ertheless, output of these metals advanced 30 and 14 percent, respectively, from 1960 to 1961. The reduction in the output of lead in the District reflects the fact that the industry is suffering from excessive stocks and over-production here and abroad. By February 1962 the price of lead had fallen ½ cent and was at its lowest level in more than 15 years. The outlook for the zinc industry appears more favorable than for lead as 1962 begins. A rise of ½ cent (East St. Louis) on December 1 for basic prime western grades of zinc was accompanied by record sales. Both industries have hopes that other countries will agree to restrict shipments of these metals to the United States when an international lead-zinc study group meets under United Nations auspices at Geneva in March.

District petroleum situation improved during year

Against a backdrop of continued general oversupply, the Western petroleum industry fared better in 1961 than in the previous year. Domestic demand for petroleum products in District V¹ increased 3.5 percent over 1960 compared with an 0.8 percent gain in the nation. Despite the improvement, marketing changes (including entrance of new firms into the area, mergers, and increased emphasis on volume sales) kept gasoline prices relatively weak, as reflected in continued outbreaks of price wars in a number of major marketing areas.

Production of crude petroleum in District V rose 0.8 percent from 1960, but receipts of crude from outside the District were up over 10 percent. In contrast, receipts of gasoline declined almost 10 percent, and production was up slightly more than 3 percent. Domestic demand for gasoline in the West was 4 percent higher than in 1960, while demand for distillate fuel rose 4 percent, and

total demand for residual fuel declined slightly.

Reflecting improved sales during the year, stocks of crude petroleum and gasoline were maintained below year-ago levels during virtually all of 1961. Stocks of distillate and residual fuel oils were generally substantially above previous year levels during most of 1961 but in each case were lowered sharply towards year end.

Record flow of cash to District farmers

The flow of income to District farmers moved up again in 1961 to record high levels. In addition to the small acreage reduction under the Feed Grain Program, modification of the cotton program reduced District cotton acreage. However, the reduction in acreage of the designated feed grains and cotton was offset, in part, by increased plantings of sugar beets resulting from larger marketing allotments of sugar to domestic producing areas. As a result, the over-all production of field crops in 1961 changed little from 1960. Production of all crops, however, increased slightly as a result of a recovery in deciduous fruit production in the Pacific Northwest and increased output of processing vegetables.

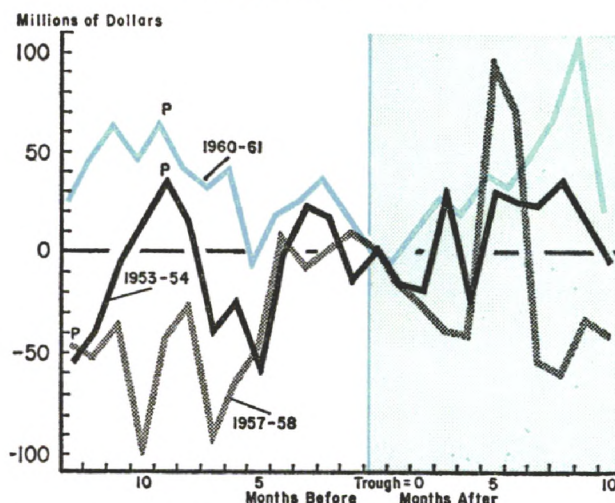
The record level of receipts in 1961 resulted from a strengthening in cash receipts from marketings of livestock and livestock products as well as crops during the latter part of 1961. In the early part of the year, the flow of income from crop marketings lagged behind a year earlier as fresh vegetable prices retreated from the unusually high level attained in the early spring of 1960. Receipts from the sale of livestock and livestock products also were at a record level in 1961; increased marketings accounted for much of the rise from 1960, although prices also strengthened during the latter part of 1961. Cash income of District farmers was further strengthened in 1961 by increased Government payments. Although payments to District farmers from the Feed Grain Program

¹ District V consists of Alaska, Arizona, California, Hawaii, Nevada, Oregon, and Washington.

were quite small, advance payments received for participation in the 1962 Wheat Program added considerably to the flow of cash to District farmers, and it appeared that sugar payments were also heavier than in 1960.

The business cycles in 1953-54 and 1957-58 were characterized by the independent movement of farm income in both the District and the nation. The lack of response to fluctuations in general business conditions during these two business cycles has been attributed to the continued high level of consumer expenditures for food, changes within agriculture (such as cattle cycles), and the effect of price supports and other Government programs for agriculture. District farm income during the most recent cycle, however, displayed a great deal more conformity with the course of general business activity than during the two previous cycles, as shown in Chart 11. Although business activity was easing throughout the year, the cash income of District farmers in 1960 rose to a record high. During the recovery and expansionary phases of the cycle in 1961, farm returns strengthened considerably in the spring of the year soon after the trough in national business activity was reached. However, the pattern of crop receipts stemming from circumstances within agriculture and changes in the Government price support program rather than the improvement in business conditions were largely responsible for this strengthening in farm income. Cash receipts were low during the early spring months of 1961 in comparison with the previous year because of unusually high prices for fresh vegetables during this period in 1960 as a result of very unfavorable growing conditions in other domestic producing areas. As marketings of 1961 crops began in volume at midyear, the increased level of price support and rising farm prices plus a somewhat heavier volume of marketings raised returns above comparable months of 1960, although crop returns for the year of 1961 were up only slightly from 1960. Hence,

CHART 11
FARM CASH RECEIPTS
TWELFTH DISTRICT



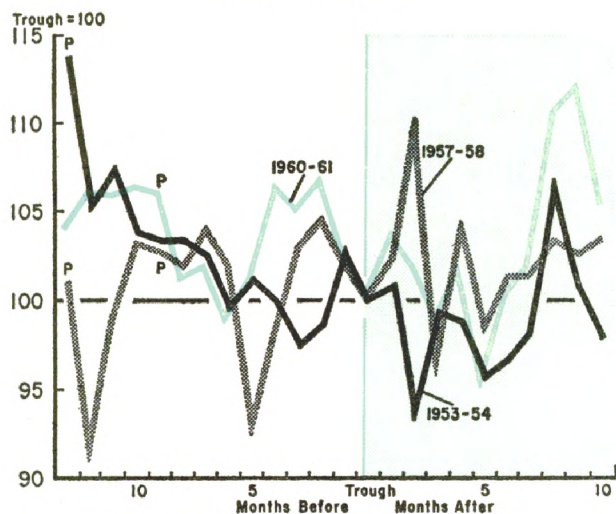
Note: In this chart, the dollar changes in monthly cash receipts from a year earlier were used instead of indexes. These dollar changes were then adjusted so that the trough month of each cycle equaled zero.
Source: United States Department of Agriculture.

evidence continues to appear in support of the position that recent business cycles have had little effect on the flow of cash to District farmers.

District canners boost output in 1961

Activity in the canning industry continued to expand in 1961, judging from available data. District canners produced a record volume of 63 million cases of canned fruit during the 1961 canning season. Vegetable canning also appeared to be heavier than a year earlier. Substantially larger packs of corn and green beans in the Pacific Northwest more than offset declines in the output of canned peas in that area and of tomatoes and tomato products in California. The increased output of canned fruit resulted, in part, from a recovery of deciduous fruit production in the Pacific Northwest, following the unfavorable growing conditions that had sharply reduced fruit output in 1960. Gains also occurred in California where increases were recorded for most major canning fruits, despite an unusually high level of inventories at the start of the 1961 canning season.

CHART 12
EMPLOYMENT IN CANNING AND PRESERVING
INDUSTRY, PACIFIC COAST STATES
(Seasonally adjusted)



Source: State departments of employment.

The volume of fruits and vegetables packed during a season appears to be little affected by fluctuations in general business activity. Food expenditures have been well maintained during recent business cycles, suggesting that domestic demand factors have been of minor importance in prompting year-to-year changes in canning activity. Supply considerations have been of greater importance in influencing the volume of canning output. These considerations relate both to the level of inventories at the beginning of the canning season and to uncontrolled changes in the supply of raw material for processing resulting from weather conditions.

Changes in important canning costs may not be directly related to changes in general business conditions. For example, the 25 percent increase in prices paid by canners for tomatoes in 1961 over 1960 resulted primarily from labor and inventory considerations directly associated with that specific activity.

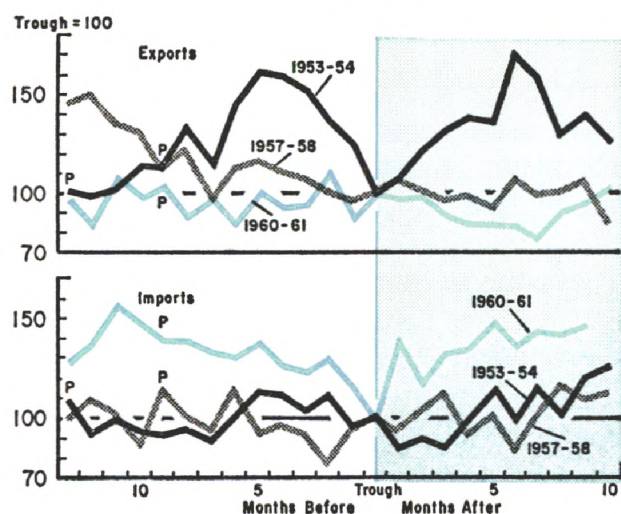
Despite the apparent independence of canning output from short-run fluctuations in general business conditions, changes in canning activity do at times influence measures

of economic well-being in the District. For example, greater than seasonal expansions or contractions in employment by canning and preserving firms, which account for 13 percent of total employment in nondurable manufacturing on the Pacific Coast, may add to or detract from the labor force or unemployment. This is illustrated in Chart 12 by the sharp rise in seasonally adjusted employment by canning and preserving firms in Pacific Coast States during the latter part of 1961 which undoubtedly aided in holding down the unemployment rate in this area. This was not the case in the 10-month recovery period beginning in May 1958 or in a comparable period beginning in September 1954 when this type of seasonally adjusted employment moved erratically and had no definite trend.

Pacific Coast foreign trade in the 1961 recovery

Merchandise exports passing through Pacific Coast customs districts in 1961, like those of the nation, contributed little to economic expansion despite an upturn in the last quarter. This is the first postwar cycle, moreover, in which West Coast exports have exerted less of a bolstering effect on the area's economy than those of the United States as a whole. The dollar value of this area's exports in 1961 was 5 percent below the comparable period of 1960, while that of the nation was 2.5 percent larger. Exports, however, remained at generally high levels as economic activity abroad, especially in the industrialized nations of Europe, continued to rise (although at a somewhat slower rate than in 1960) and in spite of the fact that a number of other countries outside Europe experienced balance of payments difficulties which necessitated some cutbacks in imports from the United States. Shipments under the United States Food for Peace Program continued to boost both District and national export totals.

CHART 13
EXPORTS AND IMPORTS
PACIFIC COAST STATES



Source: United States Department of Commerce.

The expansionary impact of Pacific Coast exports on general business activity in 1961 was the smallest of the last three recovery periods because of the leveling off in economic activity abroad. The tapering off in industrial activity abroad—and consequently in United States and Pacific Coast exports—during 1961 occurred during a less favorable phase of the business cycle which coincided more closely with the recovery in this country compared to earlier cycles. In the 1958 recovery, exports had already fallen to a plateau from the exceptionally high levels of 1957 before the upturn occurred so that they were more or less neutral, while boom con-

ditions abroad prevailed and foreign reserve positions showed marked improvement in the 1954-55 recovery, thus stimulating exports through Pacific Coast ports.

Imports, on the other hand, are influenced largely by changes in the tempo of business activity in this country. During the 1960-61 business cycle, goods entering Pacific Coast ports from abroad reacted most sharply to cyclical fluctuations in comparison with previous postwar cycles. Part of the explanation probably arose from the fact that by 1960-61 much of the impact of industrial recovery abroad from the effects of the war, with the concomitant emergence into full production of efficient, modern plant, had already been registered. Consequently, cyclical influences again became more dominant. Earlier, the cyclical behavior of our imports had been to a large extent obscured by the steadily rising trend of our purchases overseas as producers abroad gradually re-entered world markets. The latest recovery period also revealed a growing divergence in the movement of Pacific Coast and United States imports, with imports shipped into Pacific Coast customs districts undergoing a wider range of variation over the cycle. Pacific Coast imports in 1961, nevertheless, were still about 2 percent below 1960—about the same as the United States—because of a slight lag in the response of imports to the turnaround in over-all economic activity.

CONTINUED EASE IN FINANCIAL MARKETS ACCOMPANIED RECOVERY IN BUSINESS ACTIVITY

The one feature of the current recovery period which had the greatest impact on banking performance in 1961 was the continued relative ease in the money markets. In the two preceding cyclical expansions, a gradually increased pressure on bank reserve positions occurred in the early months of the upswing, as illustrated in Chart 1 on page 48 showing free and net borrowed reserves of member banks in the nation. This condition of ease was the combined result of monetary policy during 1961 (the principal aspects of which have been described at an earlier point) and a lagging demand for bank loans. The fact that the rate charged prime borrowers by commercial banks did not fall in 1961 may have played a role in the lack of marked expansion in business loans. Since open market money rates fell well below the prime rate, some borrowing may have been diverted into the commercial paper and bankers' acceptance markets. In addition, the near-record volume of new security issues sold by corporations may also have provided some funds actually employed for short-term purposes.

District loan demand lagged in 1961 recovery

Changes in loan portfolios of member banks in the Twelfth District in 1961 reflected the general expansion in business activity since the cyclical trough in February, but there was a somewhat longer time lag than usual after the trough before a clear increase in loan demand materialized. It was not until the fourth quarter of the year that loan volume definitely turned up, and even then part of the increase was due to seasonal factors, including December borrowing related to quarterly tax and dividend payments. In the 10-month period from February to the end of the year, District member bank loans¹

increased 5.8 percent. This percentage gain was less than three-fourths the rate of increase in the 10-month period after the trough in the 1958 business cycle and only one-half of that in the 1954 cycle. The mildness of the recent recession, which resulted in only a leveling off in loan volume rather than a decline, was a contributing factor to the lag in the current loan upturn and also to the relatively moderate rate of increase.

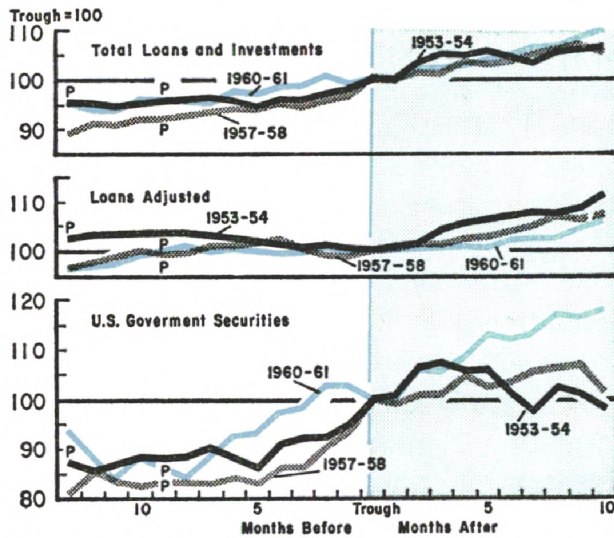
An examination of the more detailed information available for weekly reporting member banks in the District disclosed that business loans² accounted for approximately one-half of the \$698 million increase in total loans¹ at these banks in the last 10 months of 1961. About one-fifth of the dollar gain was in real estate loans, and the "other loan" category, which is composed mainly of consumer loans, showed a small decline. This latter loan category, if adjusted for repayments on consumer receivables involved in one transaction with a national retailer early in the year, would have shown an increase of about \$100 million rather than a decline. This pattern was somewhat similar to that in the 10-month period after the cyclical trough of August 1954 when business loans¹ accounted for one-half of the loan increase at District weekly reporting member banks, and the proportionate shares in real estate and "all other" loans were roughly one-fourth and one-fifth, respectively. The recent upturn contrasted with the 1958 cycle when real estate loans accounted for over one-half of the total increase in loans adjusted during the first 10

¹Exclusive of loans to domestic commercial banks and after deduction of valuation reserves.

²Including loans to sales finance companies; business loan data for the 1954 cycle also include agricultural loans.

The District banking data used in the following analysis and in the accompanying charts are not seasonally adjusted, and the difference in timing of the troughs distorts to some extent the cyclical comparisons. Data from the cyclical peak in April 1960 to December 1961 have been adjusted to include for the entire period nonmember banks that became member banks during 1960 and 1961.

CHART 14
LOANS AND INVESTMENTS OF MEMBER BANKS
TWELFTH DISTRICT



Note: Loan data consist of total loans less valuation reserves.

months after the trough, with business loans¹ contributing only one-fourth of the dollar increase in loans, and consumer loans responsible for one-fifth of the gain. Due to the generally lessened demand for residential housing in the last several years, demand for bank credit to finance real estate is not expected to be as strong in the current expansion as in other recent business cycles. At the same time, because of the increase in interest rates on time deposits and the continued heavy inflow of such deposits, banks may be expected to seek mortgages more aggressively in 1962. Reversing its neutral influence in the earlier months of the business recovery, consumer demand now appears to be an increasingly positive factor, and banks can be expected to increase their portfolios of consumer loans as sales of durable goods, particularly automobiles, continue at high levels.

Security holdings rose sharply

The most substantial change in assets of District member banks in 1961 was an increase of 19 percent in security holdings since the cyclical turning point in February. The

rate of increase was about the same for both United States Government and other securities. This gain in total investments was in sharp contrast to the 0.4 percent and 1.9 percent increases in the first 10 months of recovery in the 1954 and 1958 cycles, respectively. As a result of the sizable addition to security holdings, total bank credit¹ extended by District member banks in the first 10 months of the current upturn rose 10 percent, more than twice the rate in the corresponding periods of the 1954 and 1958 business cycle.

Steady rise in time deposits in 1961

District member banks had a steady increase in time deposits in 1961 with the level of such deposits at the end of the year 11 percent above that of February, nearly double the gain during the 10-month period following the trough in each of the two preceding cycles. Based on the performance of weekly reporting member banks, savings deposits accounted for three-fourths of the total increase in time deposits. In the second quarter of 1961 many banks, particularly in California, attracted additional funds by adopting a policy of computing interest on savings accounts on a daily basis. Demand deposits, as well as time deposits, rose gradually during the 10-month period of recovery after February, with the usual large seasonal increase in December. Discounting the December increase, the gain in demand deposits was about the same as in the corresponding periods of the two former cycles.

Bank liquidity improved

In the absence of restrictive pressure on reserves, with only a moderate increase in loan demand, and with rising deposits, Twelfth District banks used their uncommitted funds to rebuild short-term security holdings, which had been substantially reduced during the business boom that reached

¹Including loans to sales finance companies.

¹Net loans and securities.

SELECTED OPERATIONS OF THE FEDERAL RESERVE BANK OF SAN FRANCISCO

(millions of dollars)

	1961	1960	1959
Discounts			
Daily average amount held	2.5	24	38
Checks handled	131,908	119,857	116,689
Coins and currency			
Coins received and counted	129	137	136
Currency received and counted	3,946	4,361	4,075
Treasury issues			
Other than savings bonds			
Issued	6,839	6,255	6,137
Exchanged	19,923	15,771	13,630
Redeemed	8,041	8,421	7,737
Savings bonds			
Issued	466	449	410
Redeemed	689	801	946

its peak in April 1960. The ratio of short-term securities (1 year and under) to deposits increased from 1.6 percent in June 1960 to 8.3 percent at the end of 1961. The ratio of loans to deposits, another measure of bank liquidity, dropped from the high of 64.3 percent in June 1960 to 58.7 percent in December 1961. With this strengthening of their liquidity position, Twelfth District member banks are in a relatively good position to service the credit needs of the District that may arise as the current recovery progresses.

Net profits of District banks declined

With lagging loan demand and relatively stable interest rates on loans, District banks had only a slight increase in earnings on loans in 1961 compared with 1960. Their earnings on securities, however, rose by nearly the same degree as did their security holdings. The amount of interest paid on time deposits rose substantially, reflecting both the steady gain in deposits and the crediting of interest on a daily basis. Other categories of expense also rose, with the net result that the percentage increase in total expense was twice as large as the rise in earnings. As a consequence, the net profits after taxes of District

banks were about 2 percent below those in 1960.

Credit ease and increased service operations affect activities of the Federal Reserve Bank of San Francisco

Maintenance throughout 1961 of ease in money and credit markets was reflected in the operations and earnings for that year of the Federal Reserve Bank of San Francisco. One of the major effects was a substantial decline in the volume of borrowing by Twelfth District member banks. This decline is shown in the accompanying table on a daily average basis; for the year as a whole, the amount of member bank borrowing declined from \$4.4 billion in 1960 to a little more than \$700 million. This decline was also reflected in the Bank's earnings on discounts, which fell to less than one-tenth of their amount in 1960. Earnings on the Bank's share of total Federal Reserve holdings of United States Government securities also declined in 1961 by about 12½ percent from 1960, despite an increase in this Bank's allotment of these securities that occurred during the year. A fall in the general level of interest rates in 1961, however, more than offset the effect upon earn-

FEDERAL RESERVE BANK OF SAN FRANCISCO

ings not only of this increased "participation" but also of the rise in total System holdings of Government securities.

The service operations of the Bank generally continued to increase, as indicated in the table. Both the dollar volume and the number of checks processed by the Bank rose about 12 percent in 1961. However, the dollar amounts of both coin and currency handled fell in 1961. This decline reflected the effects both of a change in Federal Reserve procedures which permitted vault cash held by member banks to be fully counted as reserves and of the discontinuance of coin wrapping by this Bank in the latter part of 1960. The Bank ended the year with about 7 percent more of its Federal Reserve notes outstanding than at the end of 1960. Transfers of funds for member banks also showed a substantial rise in dollar volume.

Increased Treasury financing operations, as in 1960, contributed to gains in 1961 in the amounts of marketable United States Government securities issued, exchanged, or redeemed by the Bank in its capacity as fiscal agent for the Treasury. As has been true in the past several years, the dollar amount of United States savings bonds issued by the Bank continued to rise, though at a somewhat slower rate; the volume of redemptions continued to decline during 1961.

SUMMARY

Changes in the number of people at work provide the most comprehensive measure of over-all economic activity that is available for making comparisons between the Twelfth District and the nation. The Twelfth District fared better than the nation for 1961 as a whole in terms of average annual nonfarm employment. Nearly 100,000 more people were working at nonfarm jobs in the District in 1961 than in 1960, whereas in the nation there was a decline of almost 300,000. The rate of increase in nonfarm employment from the business trough in February 1961 was

less rapid in the District than in the nation during the first five months of recovery, but in the second half of the year the District's rate exceeded the national one. Of greater regional interest, perhaps, was the fact that, after 10 months of expansion, District nonfarm employment had risen less than 3 percent, compared with 5 to 6 percent gains during comparable periods of the 1958-59 and 1954-55 recoveries.

Almost all major industry groups in the District fared less well in terms of employment gains than in prior recovery periods. Employment in contract construction and in lumber and wood products showed almost no improvement during 1961, compared with typically sharp gains in the two preceding recoveries. This reflected primarily the more limited and late revival in residential construction in 1961 as compared with the earlier periods.

The 4 percent growth in manufacturing employment in the 10 months of recovery was less than half as large as the increases in the two prior periods, despite sharp advances in both durable and nondurable goods industries in the latter half of 1961. In the Pacific Coast States, where District manufacturing is concentrated, the annual average manufacturing employment in 1961 was slightly below the 1960 level. Only four industry groups were above the 1960 level, and two of these were defense-related, shipbuilding and electrical equipment.

One of the important restraining influences upon manufacturing employment in both the District and the nation was the fact that the level of total retail sales showed comparatively little increase until late in the year. Personal income grew at a considerably faster rate than retail trade, reflecting perhaps some feeling of uneasiness by consumers concerning the outlook in view of the continued high unemployment rate.

Although the production of steel and nonferrous metals in the District did not rise as

rapidly during the recovery in 1961 as in the two prior recoveries, it is significant that output for the year as a whole was higher than in 1960 in each case. Primarily because the District steel industry is less dependent upon automobile production, its output has typically been more stable during the postwar business cycles than has national production. District producers of nonferrous metals were considerably affected by factors not directly associated with the domestic business cycle. At the end of the year, a favorable aspect in the outlook for copper was the relatively low level of inventories, and zinc sales reached record levels in December, reflecting in part a rise in price at the start of the month. The lead industry, however, is suffering from excessive stocks and overproduction here and abroad, with the result that in early 1962 its price dropped to the lowest level in 15 years.

Farm income in the District, as in the nation, fared well in 1961, rising to a new record. The canning industry, which is an important employer in the District, also turned out a record pack of fruits and vegetables. Neither farming nor canning in the District has been particularly affected by recent business cycles, largely because consumer buying of food has been well maintained even in periods of recession.

The volume of merchandise exports passing through Pacific Coast ports is primarily responsive to changes in business conditions abroad rather than in this country. With some slowing down in the rate of business expan-

sion abroad, exports from District ports in 1961 dropped below the 1960 level. Imports through District ports were also below 1961, reflecting some lag in the response of imports to the domestic recovery which occurred in the last 10 months of 1961.

The general ease in the reserve position of banks and in financial markets generally permitted District banks to improve their liquidity position significantly from the low level that developed in mid-1960. This should enable the banks to meet rising credit demands as the recovery progresses, although no clear-cut evidence of a marked upsurge in loan demand had developed in the early months of 1962.

In conclusion, it is clear that District business activity by the end of 1961 had made a significant recovery from the low point in February, with much of the increase concentrated in the second half of the year. However, some hesitation in the rate of recovery occurred in both the District and the nation in the first two months of the new year. This, coupled with the fact that the District's recovery has so far been considerably less vigorous than in the prior two cycles, provides the basis for some indecision at this point in time. Although it is not yet clear whether the tiger or the pussycat will prove to be the more appropriate symbol for indicating the strength of District business activity in 1962, at the moment it does appear that it will at least require a very large cat.



FEDERAL RESERVE BANK OF SAN FRANCISCO
BANKING AND CREDIT STATISTICS AND BUSINESS INDEXES—TWELFTH DISTRICT¹
(Indexes: 1947-1949=100. Dollar amounts in millions of dollars)

Year and Month	Condition items of all member banks ^{2, 7}				Bank debits index 31 cities ^{4, 5}	Bank rates on short-term business loans ^{6, 7}	Total nonagricultural employment	Total mfg employment	Car-loadings (number) ⁸	Dep't store sales (value) ⁸	Retail food prices ^{7, 8}
	Loans and discounts	U.S. Gov't securities	Demand deposits adjusted ³	Total time deposits							
1929	2,239	495	1,234	1,790	42	....	...	...	102	30	64
1933	1,486	720	951	1,609	18	....	...	...	52	18	42
1939	1,967	1,450	1,983	2,267	30	....	60	57	77	31	47
1952	8,839	6,619	10,520	7,502	140	3.95	118	130	100	120	115
1953	9,220	6,639	10,515	7,997	150	4.14	121	137	100	122	113
1954	9,418	7,942	11,196	8,699	153	4.09	121	134	96	122	113
1955	11,124	7,239	11,864	9,120	173	4.10	127	144	104	132	112
1956	12,613	6,452	12,169	9,424	190	4.50	134	154	104	141	114
1957	13,178	6,619	11,870	10,679	204	4.97	139	161	96	140	118
1958	13,812	8,003	12,729	12,077	209	4.88	138	153	89	143	123
1959	16,537	6,673	13,375	12,452	237	5.36	146	165	94	157	123
1960	17,139	6,964	13,060	13,034	253	5.62	150	165	88	156	125
1961	18,499	8,278	14,163	15,116	270	5.46	152	163	87	175	127
1961											
February	17,525	6,991	12,750	13,639	256	....	150	161	83	164	127
March	17,517	6,916	12,860	13,754	273	5.48	150	161	83	160	127
April	17,637	7,436	13,222	13,999	266	....	150	160	88	164	127
May	17,632	7,393	12,865	14,289	265	....	151	162	81	153	127
June	17,578	7,571	12,935	14,371	268	5.50	152	163	85	162	126
July	17,504	7,935	13,206	14,492	267	....	152	162	86	167	126
August	17,779	7,863	13,212	14,656	262	....	152	164	84	157	125
September	18,028	7,955	13,317	14,786	277	5.45	153	165	87	170	126
October	17,901	8,190	13,901	14,867	291	....	153	166	99	164	127
November	18,212	8,182	13,944	14,874	265	....	154	167	100	165	126
December	18,499	8,278	14,163	15,116	293	5.42	154	167	92	175	127
1962											
January	18,646	8,082	13,671	15,448	294	....	155	169r	100	166r	127
February	18,622	7,820	13,163	15,647	289	....	156p	169p	99	176	128

Year and month	Industrial production (physical volume) ⁵							Waterborne Foreign Trade Index ^{9, 10}					
	Lumber	Petroleum ⁷		Cement	Steel ⁷	Copper ⁷	Electric power	Exports			Imports		
		Crude	Refined					Total	Dry Cargo	Tanker	Total	Dry Cargo	Tanker
1929	95	87	78	55	...	103	29	190	150	247	124	128	7
1933	40	52	50	27	...	17	26	110	...	...	72	...	...
1939	71	67	63	56	24	80	40	163	107	243	95	97	57
1951	113	106	112	128	146	116	136	186	194	175	162	140	733
1952	115	107	116	124	139	115	145	171	201	130	204	141	1,836
1953	116	109	122	131	158	113	162	141	138	145	314	163	4,239
1954	115	106	119	133	128	103	172	133	141	123	268	166	2,912
1955	122	106	124	145	154	120	192	166	178	149	314	187	3,614
1956	120	105	129	156	163	131	209	201	261	117	459	201	7,180
1957	106	101	132	149	172	130	224	231	308	123	582	216	10,109
1958	107	94	124	158	142	116	229	176	212	123	564	221	9,504
1959	116	92	130	174	138	99	252	188	223	138	686	263	11,699
1960	110	91	134	161	154	129	271	241	305	149	808	269	14,209
1961	109	92	140	169	171	136	...	...	...	...	...	...	...
1961													
January	100r	91	134	159	131r	139	277	235	318	118	779	218	15,394
February	100r	91	134	176	152	134	276	248	362	95	666	233	11,985
March	103	92	131	178	162	137	285	264	363	124	952	252	19,268
April	114	92	135	168	172	133	283	261	331	163	759	286	13,139
May	111	92	143	169	191	143	285	265	331	171	865	292	15,856
June	111	91	143	188	187	143	289	224	290	128	767r	289r	13,223r
July	110	91	143	157	183	124	293	271r	365r	138	1,026r	297	20,025
August	111	91	140	160	180	107	300	247	322r	140r	805r	277r	14,586i
September	111	92	142	163	174	138	295	217	317	76	841r	277	15,542
October	110	92	144	171	181	149	310	209	310	67	872	307	15,613
November	113	92	144	182	167	147	305	256	331	148	756	264	13,573
December	106	92	141	152	167	145	...	...	...	...	...	...	...
1962													
January	...	90	139	165	184	143	...	...	...	...	...	...	...

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