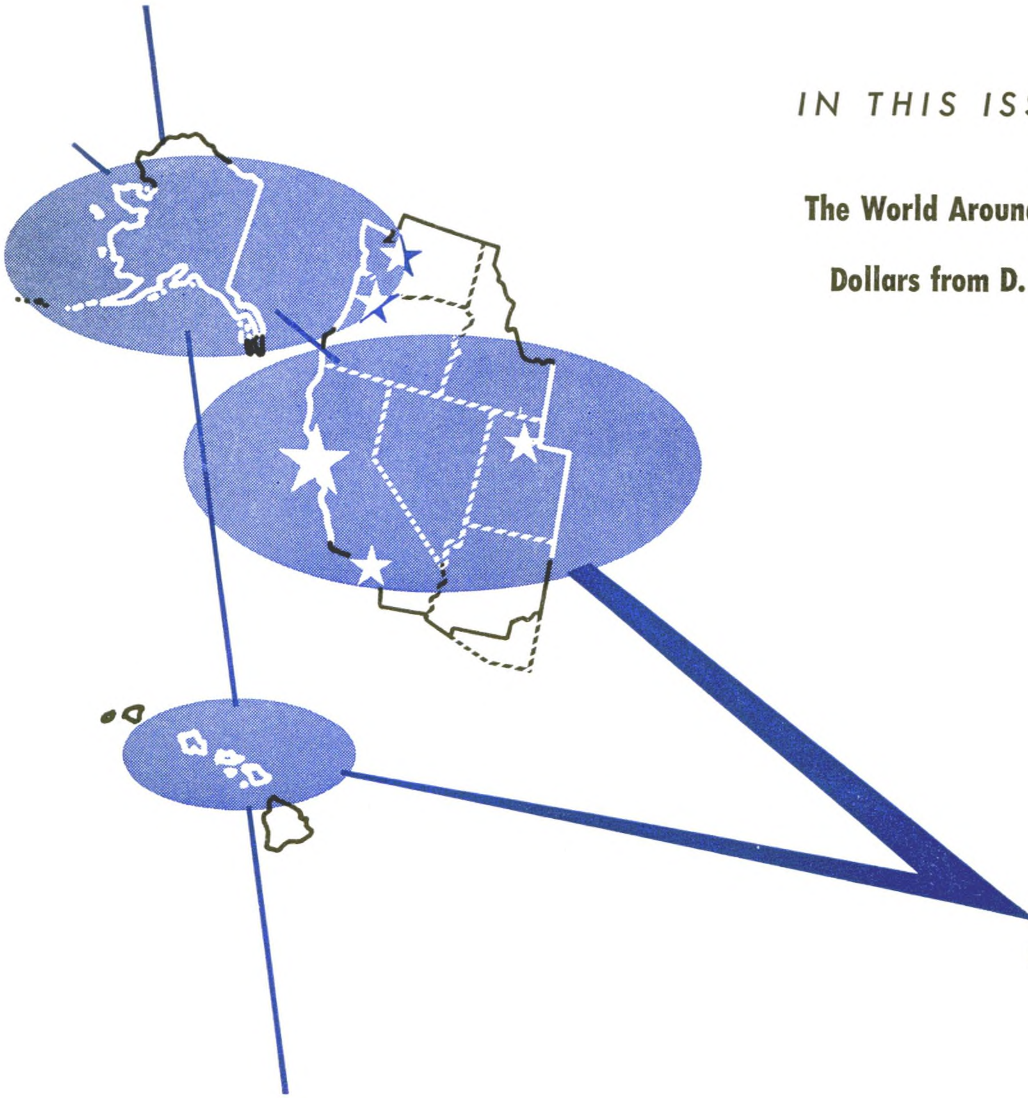
FEDERAL RESERVE BANK OF SAN FRANCISCO

MONTHLY REVIEW



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FEBRUARY
1965

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. . . Despite the sterling crisis, 1964 witnessed substantial progress in the production, distribution, and financing of worldly goods.

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. . . Federal grants help fill the gap between the growing needs and limited resources of state and local governments.

The World Around Us

DURING the course of 1964—the first of two International Years of the Quiet Sun—outer space became increasingly populated with flying or orbiting objects. The new satellites, known by such adventurous-sounding names as Syncom, Ranger, Mariner, and Explorer, joined Telstar and Vanguard (ours), Cosmos (theirs), and other pioneers in space. In addition, the Russians outdid both themselves and us by successfully launching the first multi-manned space vehicle, appropriately dubbed Voskhod ("sunrise"). With all these foreign objects whirling around in space or hurtling at great speeds toward the moon or Mars, attention may easily have been diverted from the more mundane happenings around us.

Even so, events on Earth, although much less spectacular, were no less important for those concerned with the production and distribution of worldly goods and with international financing. Before the onset of the sterling crisis in the last quarter of the year, gratifying progress had been made toward internal and external balance in most of the industrial countries of the world and also in many of the less developed areas. Payments surpluses or deficits were reduced in many countries; inflationary pressures were generally held under control; money and capital markets abroad were further broadened and liberalized; and international economic and financial cooperation was strengthened.

These developments benefited the U. S. balance of payments position, as well as the position of other areas. After all, pressures on deficit and surplus countries are lessened and more easily borne when no country's position is excessively unbalanced in one direction or another. Balanced economic expansion, furthermore, gives all countries a chance to share in a rising volume of trade and facilitates the most efficient allocation of resources and mobilization of savings.

Not surprisingly, then, U. S. exports and the export surplus rose sharply last year—at least through the first three quarters—in response to high levels of business activity abroad. In addition, capital outflow into portfolio investments slowed, partly due to the inhibiting effects of the interest equalization tax but also to the opening up of overseas capital markets to a larger volume of foreign security issues. Developments abroad were not wholly favorable, however, and the seeds of possible future distortions were by no means completely removed.

Toward a solution in Britain?

The most unfavorable development was the sterling crisis which occurred in the final quarter of 1964. The British balance of payments situation had deteriorated rather steadily throughout the year, as unfavorable export-import developments and sizable long-term capital outflows were reinforced by growing uncertainties about the underlying strength of sterling. But the crisis was precipitated not so much because of any new evidence regarding a weakening of the nation's basic economic position, but rather because of a financial crisis of confidence brought on by the growing payments deficit and the imposition of a system of import surcharges.

The recent inadequate economic performance of the United Kingdom, in comparison with that of other industrial countries (especially those in continental Europe), is the outgrowth of developments over a long period of time. The U. K. economy has fallen behind in its rate of economic growth, in exports, and in technological innovation. Long-entrenched labor and business practices have tended to obstruct essential modernization and rationalization of British industry and to weaken Britain's competitive position in both domestic and foreign markets.

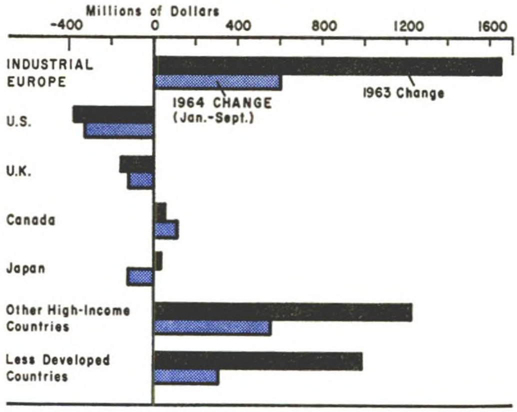
The present situation did not develop overnight and is of such a nature that it will take time to correct. But the resources are there. Given the necessary determination, Britain's economic position can be strengthened without placing unbearable pressures on other countries.

Toward international balance

Apart from the U. K. situation, 1964 generally was a successful year for world trade and finance. Judging from January-September changes in international reserves, which constitute the most current indicator of balance of payments trends, pressures stemming from substantial payments deficits or surpluses moderated somewhat in 1964. Anti-inflationary programs, measures curbing inflows of capital or encouraging capital exports, and intended or unintended increases in imports resulting from internal price pressures—all of these contributed to the move toward international balance. (Subsequent disturbances in the exchange markets in connection with the sterling crisis make final-quarter changes in reserves misleading as a measure of basic payments developments.)

The payments surpluses of France, Germany, Switzerland, the Netherlands, and Belgium were much reduced, or even eliminated in some cases. Accumulation of gold and foreign exchange reserves was slower for countries such as Austria, Denmark, and Australia. At the same time, Italy succeeded in halting the drain on its international reserves as credit restraints contributed to a rapid improvement in its trade balance. Japan's austerity measures also helped reduce its payments deficit, although it still recorded a net loss of reserves for the year as a whole. Canada, Spain, Sweden, and New Zealand also fared better than in 1963. The United States and the United Kingdom supplied reserves to the rest of the world through reductions in their monetary reserves and additions to their

International reserve accretions and losses slower in 1964



Note: Industrial Europe includes Common Market, Sweden, and Switzerland; other high-income countries include rest of Western Europe, Oceania, and South Africa; less developed countries include all other countries not shown on chart.
Source: International Monetary Fund

liquid liabilities to foreigners. Dollar liabilities to foreigners, however, grew less rapidly than sterling liabilities.

During the January-August period, a strong degree of confidence in the international economic and political situation bolstered official holdings of gold, as less of the new gold supply moved into private hands. Additions to existing Free World gold stocks came from new production, largely from South Africa, and from Russian gold sales to finance grain imports. In contrast to 1963, most of these net additions to foreign official holdings of gold did not come from U. S. stocks or from the already-depleted British gold stocks. As the sterling crisis developed, however, private demand for gold increased, and most of the new gold probably moved into private hands after August. Preliminary estimates place the rise in private holdings in 1964 around $1 billion, as a result of both industrial and hoarding demand.

The relative calm on the international scene in the first nine months of the year was reflected in a relatively steady London gold price; the only price flurries were associated with such events as the rumor of an impending devaluation of the Italian lira, the illness of the Greek king, the British election, and occasional tensions in the Middle East. Additional steadiness was imparted by the Russian gold sales and operations of the London gold pool, which acquired sizable amounts of gold in the first half of 1964.

But the run on the pound which began in late September upset the previous stability of the gold market. Gold prices moved up as high as $35.19 in unofficial dealings by late December—exacerbated by inaccurate market reports of prospective French conversions of their dollar holdings into gold—before subsiding in the face of a strong U. S. Treasury statement which emphasized this nation's confidence in the pound and reiterated its determination to maintain the gold price. During this period, the London gold pool was probably a net supplier to the market, in contrast to the first half of the year, when the U. S. acquired a substantial amount of gold as a result of its 50-percent participation in the pool.

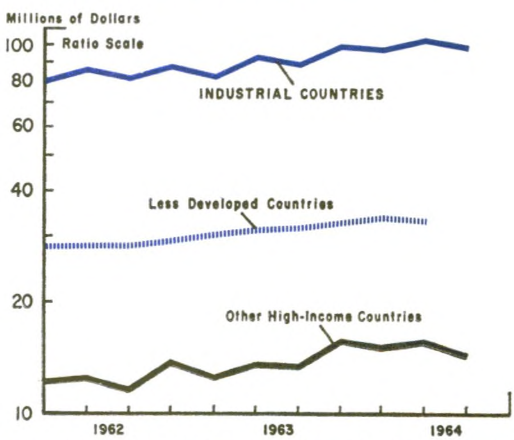
Toward foreign-trade expansion

The expansion of world trade in 1964 continued to contribute to international payments equilibrium. Countries with large trade deficits, such as Japan and Italy, or countries with sizable export surpluses, such as Germany, were able to bring their trade imbalances down to reasonably manageable proportions toward the end of the year. (In some cases, however, success in reducing imports had unfavorable repercussions on the exports of another major trading country; the decline in Italy's imports, for example, was strongly felt by the U. K.) Where capital inflows had been an important factor in international reserve gains in 1963, as in the case of France, the Netherlands, and Belgium, changes in the merchandise trade balance last year worked in an offsetting direction.

Among other major industrial countries, Canada and the United States increased their trade surpluses, while the U. K. trade balance deteriorated as a result of a disappointing export performance and unexpected strength in imports, which was partly related to uncertainties surrounding the future of sterling. Export earnings of the less developed countries as a group tended to fall off during the year because of the leveling off in economic expansion in the leading industrial countries and because of some weakening of international commodity prices.

Japan liberalized its import policies, as a condition for its move to currency convertibility for transactions by nonresidents in goods and services (under the provisions of Article VIII of the IMF charter). Germany, Austria, and Spain also liberalized for anti-inflationary reasons, following the example of France and Italy the year before. Progress also was made in the preliminaries to the "Kennedy Round" of talks for tariff re-

Exports continue to expand
throughout most of 1964



Note: Chart shows quarterly data at annual rates, unadjusted for seasonal variation; industrial countries include industrial Europe, U. S., U. K., Canada, and Japan; for other definitions, see first chart.
Source: International Monetary Fund

ductions. The Common Market countries agreed on a common price for cereals (which paved the way for the inclusion of agricultural commodities in the current negotiations), and the U. S. and the Common Market submitted relatively abbreviated lists of products to be excepted from the proposed reductions in industrial tariffs. As with many developments during the year, however, progress was not completely free of complicating factors. Higher grain prices within the Common Market will boost production in the area, but will weaken this country's competitive position because the high support levels will have the effect of increasing the landed cost of American wheat.

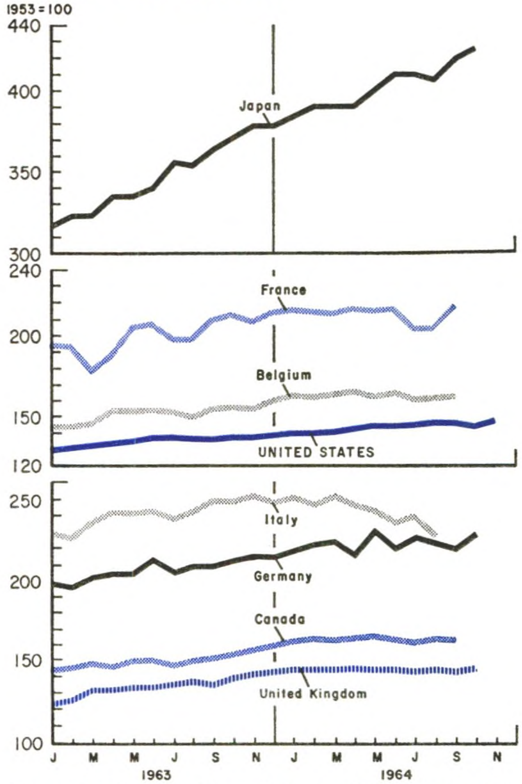
Toward internal equilibrium

The pace of economic expansion moderated somewhat in the industrial countries in 1964 as inflationary pressures stemming from manpower and capacity limitations and balance of payments problems slowed the rate of advance. Production in the United Kingdom, Canada, Belgium, and France leveled off after some increase earlier in the year. Japanese output continued to move up despite maintenance of credit restraints, but recessionary tendencies emerged in Italy as the deflationary measures adopted earlier began to take hold.

Consumer demand tended to weaken in most industrial countries except Germany. Investment demand remained steady at high levels (except in France and Italy), although construction activity tapered off after an upsurge early in the year. Exports generally were a less expansionary force than in 1963, and were decidedly unsatisfactory for the United Kingdom. Labor market tensions heightened in a number of countries and contributed significantly to upward price pressures, particularly in the Netherlands and Germany.

Price indexes reflected the net impact of

Output abroad grows less rapidly in 1964 than in 1963



Source: Organization for Economic Cooperation and Development. International Monetary Fund.

these market forces. Anti-inflationary measures helped dampen price increases in France, but similar measures were less successful in Italy. Prices continued to increase in Japan and the Netherlands, and around midyear the indexes began to accelerate in the United Kingdom and Belgium. Price pressures were further reflected in money market rates.

To combat inflationary pressures, leading countries took a number of steps to raise the cost and reduce the availability of credit and to dampen demand and cost pressures. The conventional instruments of monetary restraint—increases in central-bank discount rates and increases in commercial-bank reserve requirements—were employed in both industrialized and developing countries. In many instances, these measures were reinforced by various types of selective credit controls, such as penalty discount rates, more stringent rediscount quotas, ceilings on bank credit expansion, greater selectivity in lending, and tightening of consumer credit terms. In addition, they were reinforced in the Netherlands, Belgium, and France by the adoption or extension of price ceilings.

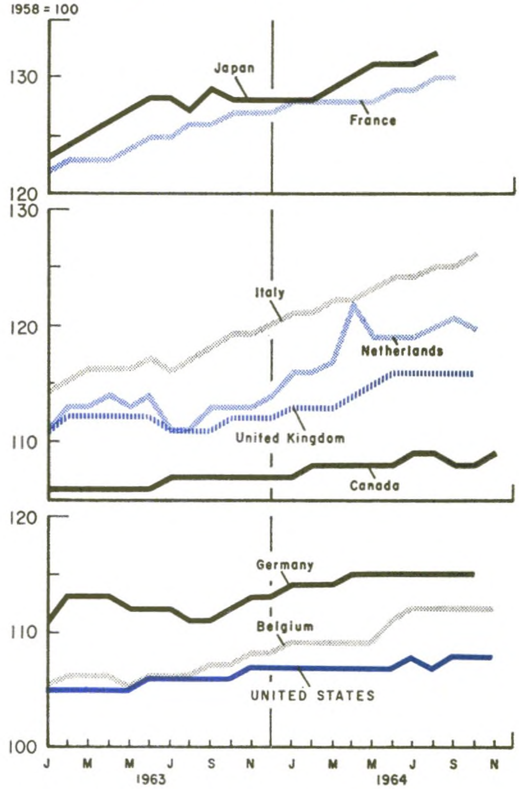
To forestall inflows of funds from abroad that would tend to nullify credit restraints, several nations introduced regulations requiring banks to match specified proportions of their foreign liabilities with foreign assets. (Nevertheless, tight domestic credit conditions encouraged banks in the Netherlands and Belgium to repatriate funds from abroad during most of 1964.) Fiscal policy was increasingly employed to bolster the fight against inflation. Budget expenditures were cut back wherever possible, and Government security issues were floated to absorb excess liquidity.

Toward increased liquidity

The resultant structure of interest rates in the major industrial countries tended to encourage capital outflows from the United States toward countries with favorable growth patterns and higher interest rates. But the interest equalization tax helped to keep down the movement of U. S.-owned long-term funds into portfolio investments abroad, while narrow money markets abroad and foreign restrictions on short-term capital inflows helped to keep short-term flows in check. But the United Kingdom—until the sterling crisis—and Canada continued to attract considerable amounts of American short-term money.

The interest equalization tax also helped to broaden and liberalize foreign money and capital markets during the year. The volume of foreign capital issues offered in European capital markets in 1964 was probably more than $1 billion—about double the average

Prices continue to advance
in most industrial countries abroad

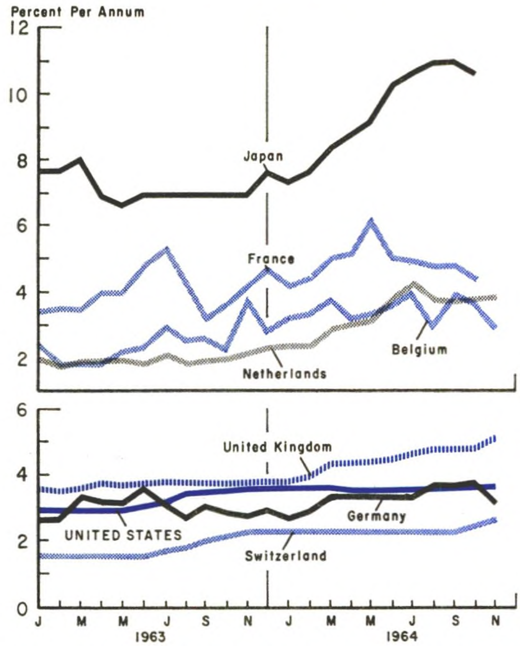


Source: European Economic Community, United Nations

for the past few years. Non-Commonwealth countries increased their borrowing in the London capital market, while foreign issues sold in Germany or denominated in Deutsche marks reached a sizable volume. At the same time, a number of countries—particularly France and Italy—attempted to increase the efficiency of domestic money and capital markets, to encourage individual saving, and to enhance the attractiveness of long-term investments to the individual investor.

These developments were decidedly favorable. Over the longer run, the increased capacity of each country to meet its own needs for investment funds and eventually to supplement the financial resources of countries less advantageously placed will reduce the

Rising money market rates
reflect inflationary pressures



Source: Organization for Economic Cooperation and Development

drain on the few countries that today supply the bulk of financial assistance to the developing countries.

The greater accessibility of foreign capital markets in 1964 increased private international liquidity and thus reduced the need for official reserves. A significant amount of international liquidity also was made available to the monetary authorities of various countries encountering payments difficulties over the year. International assistance—either in the form of drawings on the International Monetary Fund or central bank credits—was provided on a substantial scale to Italy in March and to the United Kingdom in the autumn sterling crisis. The Fund's General Arrangements to Borrow—a supplementary $6-billion standby credit arrangement concluded in 1962 among ten industrial countries—was activated for the first time in November in connection with the U. K. $1-billion drawing from the Fund. In addition, the network of Federal Reserve swap arrangements with foreign central banks and the Bank for International Settlements was used by the U. S. and other countries to meet temporary strains in the international exchange markets.

In September, at the annual meeting of the International Monetary Fund in Tokyo, IMF members agreed in principle to the expansion of liquidity through a general—but as yet unspecified—increase in member country quotas. In addition, the "Group of Ten" industrial countries instituted a system of "multilateral surveillance"—involving the regular reporting of official means of financing payments deficits and surpluses—to facilitate balance of payments adjustments.

Toward the future

The outlook for 1965 for the major industrial countries abroad is generally favorable. The overall pace of expansion is expected to be somewhat slower than in 1964, but there should be further progress toward a balanced development of the various sectors of each nation's economy. Current efforts to restrain inflationary pressures should tend to keep price increases smaller than in 1964. Japan, however, has already begun to ease its policy of credit restraint, and Italy is contemplating measures to stimulate its sagging economy.

Investment demand is generally expected to rise at a brisker pace than in 1964, but consumer demand may be less expansionary in most countries except Germany. In addition, increases in output may be dampened by capacity limitations, particularly in Germany and Belgium, and by the intensification of labor shortages in most countries other than Italy and France. Common Market experts forecast only a 3-percent gain in output in the first quarter of this year above the year-ago period, compared with a 10-percent gain in the comparable 1964 period. Productivity gains for industrial countries (other than

France) are expected to be less easily achieved this year.

Meanwhile, fiscal policy in the industrial countries continues to be tailored to the requirements of anti-inflationary programs, with government expenditures and budget deficits smaller than in 1964. The French budget for the current fiscal year, for example, is expected to register a small surplus for the first time since the late 1920's.

The payments position of most countries—whether in surplus or deficit—should be less lopsided in 1965, according to various official and semi-official estimates. The impact of the import surcharges on U. K. imports should be felt early in 1965, but it will probably take longer for exports to respond to current measures designed to stimulate sales abroad. The German trade surplus may be about as large as last year as exports level off and imports rise, but capital exports may increase. In Belgium, a slower rise in exports may be accompanied by a slower rise in imports. For the remaining industrial countries (except Japan), export demand may pick up while imports may rise more slowly; in Japan, current low levels of inventories point to possibly sizable replenishment of stocks from abroad. In the less developed countries, meanwhile, export earnings may show little further improvement, but the attainment of a more comfortable reserve position in 1963-64 may permit some increase in imports.

In general, continued progress can be expected in 1965 toward internal and external equilibrium. Formulation of an effective program for strengthening the U. K. economy and restoration of confidence in the pound merit top priority, both for the U. K. itself and for the whole international payments system. Other new problems will of course arise from time to time, but 1964 provided ample evidence that the nations of the world have become more flexible, adaptable, and better equipped to meet contingencies as they arise. Meanwhile, as satellites hurtle through the void in their search for solutions to the mysteries of outer space, and as ministers hurtle from capital to capital in their search for a better system of international payments, the world's trade surges steadily ahead.

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Dollars from D.C.

BEFORE LEAVING the tumult of Washington for the hurly-burly of academic life, Professor Walter Heller sparked a new tax debate by proposing that the states receive an automatic distribution of some Federal revenues every year. Under the Heller plan, the Federal Government would assist the state and local governments, beset as they are by the necessity of meeting rapidly expanding public needs out of comparatively restricted tax systems, through automatic transfers of Federal tax revenues to be used at the discretion of the individual states.

The future of the Heller proposal is certainly problematical, in view of the possible reluctance of Congressional and Administration leaders to relinquish fiscal responsibilities to other jurisdictions, and again in view of the objections of administrators of present programs to the channeling of funds to other uses. But whatever the fate of this proposal, the transfer of increased amounts of Federal revenues to state and local governments through ongoing programs seems assured.

The Federal grant-in-aid system, an existing system which lacks only the automatic and discretionary features of the Heller plan, has already assumed a major role in the revenue structure of state and local governments. Throughout the postwar period, this type of intergovernmental expenditure has been largely responsible for filling the gap between the needs and resources of state and local governments, and for making possible the growth and improvement of public services which have been achieved in those jurisdictions.

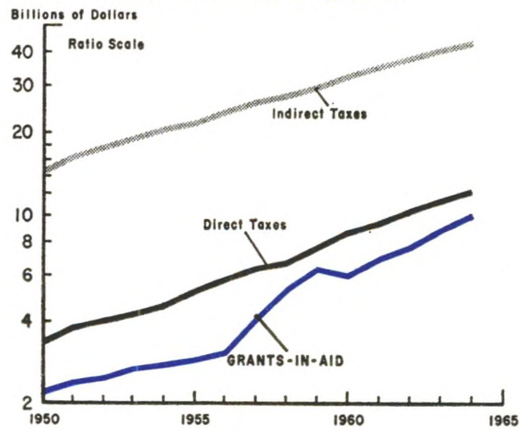
Growth of grants

In 1963, state and local governments were able to raise twice as much revenue from their own sources as they did a decade earlier, but their income from Federal grants more than tripled during the same period. Between 1957 and 1963 alone, the income from grants more than doubled. The variety of grant programs has also increased steadily; by April 1964, the "Catalog of Federal Aid to State and Local Governments" listed authorizations for Federal assistance to state and local governments under 115 different programs.

State revenue from the Federal government increased from \$3.5 billion in 1957 to \$7.8 billion in 1963, and Federal grants thus rose from 18 to 23 percent of total general revenues of state governments. The greatest increase in recent years has been grants for highway construction and related activities, which more than tripled in the 1957-63 period. The interstate highway program accounted for much of this growth. During the same period, grants to states for education increased by more than 170 percent, and grants for state health and welfare programs grew by nearly 75 percent.

State grants to the various units of local government have grown in line with the revenue that state governments have been able to

State-local budgets rely increasingly on Federal grants



Note: Chart shows all sources of state-local government receipts except contributions for social insurance.
Source: Department of Commerce

raise from their own sources. State grants to municipalities traditionally have been larger than the total volume of Federal grants—fortunately so, since the financial resources available to local governments are less easily expandable than are the financial resources of state governments. For example, property taxes are by far the most important source of tax revenue for local governments, but any increase in the revenue which can be raised from this source is strongly dependent upon increases in property values. (Property tax revenues have recently kept in step with revenues from other sources, however, as a result of increases in assessments and in tax rates as well as increases in property values.)

State grants to local governments increased from \$7.3 billion in 1957 to \$11.9 billion in 1963, in each year amounting to about 30 percent of the total general revenue of local governments. Most of the increase was in grants for education and health and welfare. Meanwhile, a small reverse flow of grant money has shifted from local governments to state governments, but this has accounted for only about 1 percent of the income of state governments.

Not surprisingly, the increase in the intergovernmental flow of funds has been especially high in the West. Between 1957 and 1963, the volume of Federal grants to state and local governments in the Twelfth District increased 145 percent. During that period, the contribution of Federal grants to the total general revenue of all District government units increased from 12 to 16 percent.

Grants to state governments in the District from the Federal government increased more than 150 percent between 1957 and 1963. Grants to states for educational purposes showed the greatest increase, more than tripling over the period, but highway and health and welfare programs grew almost as rapidly. In each specific case, Federal grants grew by more than state direct expenditures.

Revenue from the Federal government financed more than 40 percent of the direct expenditure of Twelfth District states in 1963, compared with slightly over 30 percent in 1957. Highway grants showed the greatest proportionate increase, but the growing importance of grants for financing state expenditures for education and welfare and health was also apparent.

Why grants?

Generally speaking, the Federal system of grants-in-aid contains a variety of specific grants geared to specific programs, but with some differences in operational detail. Although a few Federal grant programs allow administrative discretion to determine the allocation of funds, most of the authorizations for such programs enumerate detailed conditions for fund allocation. A given grant program usually contains two provisions to determine the share of funds each state will receive: one provision regarding the manner in which the appropriations for the program will be apportioned among the grantees as an offering of Federal aid, and another provision regarding the funds to be raised by each grantee for its share of the project. The distribution of Federal grants is thus a function of the program needs, the financial needs, and the fiscal capacities of eligible recipient governments. In addition, the willingness of state and local governments to increase revenues in order to obtain matching funds is also a significant factor.

Basically, grant programs are undertaken as a means of redistributing fiscal resources in order to induce recipient governments to undertake programs deemed socially desirable by the Federal and state governments. However, grants-in-aid are also a means of narrowing the gap between the fiscal needs and the fiscal resources of state and local units of government. The taxing and borrowing powers of local governments are limited by a myriad of constitutional and statutory restrictions; local governments, deriving their fiscal powers from the state, are generally dependent upon property taxes as their major source of tax revenue. State governments, although possessing much more extensive tax resources than local governments, are still somewhat more restricted than the Federal Government in their ability to raise funds. In principle, then, grants-in-aid permit the collection of revenue from the most effective and efficient tax base, and the execution of governmental activities at the most efficient and effective level.

Intergovernmental expenditure affects both the level and the direction of state and local government spending. Federal aid usually calls forth more expenditure than the amount of the additional revenue it provides, because matching requirements generally oblige state and local recipients to provide a certain proportion of the money to finance any given project. Grants also affect the direction of state and local government spending, since all Federal grants and most state grants are authorized for specific uses in specific programs.

The intergovernmental flow of funds includes more than just grants-in-aid in the strict sense of "gifts" (conditional or unconditional) from one governmental unit to another. Revenue-sharing is another possibility; for example, states in which national forests are located receive 25 percent of the revenues from the operation of those forests by the Department of Agriculture's Forest Service. In addition, loans, advances, and technical assistance provide other types of intergovernmental aid.

For what purpose?

In fiscal 1963, 39 percent of total Federal aid to state governments consisted of highway grants. Another 35 percent of total Federal aid went for public welfare, and yet another 15 percent for education. Other important uses of grants were employment security administration, health and hospitals, natural resources, and airports.

State grants are made to all types of local governments — counties, municipalities, school districts, townships, and special districts. More than half of the intergovernmental expenditure of states goes to school districts, while counties and municipalities receive most of the remaining portion of state aid. States generally follow the Federal practice of utilizing grants to finance specific nonrecurring expenditures such as construction and research, but fully one-twelfth of state grants are made for "general local support."

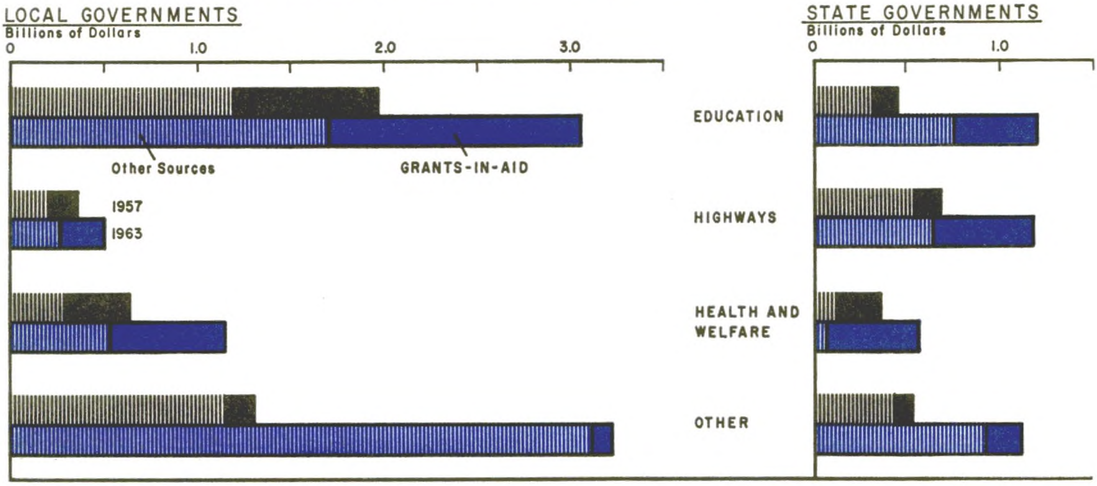
Education is by far the most important function financed by state aid; in 1963, for the nation as a whole, 59 percent of state grants were made for that purpose. In the same year, public welfare accounted for 16 percent of the intergovernmental expenditure of states, and highway grants accounted for 12 percent more.

District patterns

In the West, the Federal Government supplied about 16 percent ($1.8 billion) of the $11.6 billion of the total general revenue of state and local governments in 1963. In addition, state grants totaling $2.5 billion accounted for a third of the general revenue of the District's local governments.

In 1963, revenue from Federal grant-in-aid programs accounted for more than 40 percent of the total direct general expenditures of Twelfth District states—a substantially higher level than the rest of the country. These Federal grants financed about 37 percent of the states' expenditures for education, 44 percent of highway expenditures, and 90 percent of expenditures for health and welfare. State governments actually received much more in public welfare grants than they spent directly, since many of their welfare expenditures were incurred for activities carried out at the local level.

Western communities demand more schools, roads, health and welfare . . . funds obtained from own taxes and from intergovernmental flow of funds



Source: Bureau of the Census (Twelfth District data)

Federal grants to local governments in the West are much smaller in volume than Federal grants to states. In contrast to the pattern in the rest of the country, however, school districts in Twelfth District states received by far the largest proportion of Federal grants to local governments—more than half of the total received by all units of local government.

The pattern of state grants to the various units of local government in the West also differs from the pattern in the rest of the country. A larger proportion of the total intergovernmental expenditure by Twelfth District states is made for health and welfare (more than one-fourth of the total, compared with less than one-sixth elsewhere), while a smaller proportion is allocated for education (54 percent, compared with 60 percent) and for highways (9 percent, compared with 13 percent).

The role of Federal grants in each individual state varies in line with its distinctive needs. In most District states, the largest portion of state revenues from the Federal government in fiscal 1963 was spent for highway construction and related activities. In Arizona, Idaho, Nevada, and Oregon, highway grants accounted for more than half of total Federal grants to states. But in California, which received the vast bulk of the District's share of Federal aid, one-third of state revenue from the Federal Government was spent on health and welfare, one-third on education, and only one-fourth on highways.

In sum, grant programs have provided an equitable method of financing projects (such as highway construction) in which national objectives are involved, and they have also stimulated state-local activity in such projects. They have provided a means of stabilizing state-local revenues, of extending assistance in recession periods, and of distributing tax proceeds collected at the most appropriate level of government to the jurisdiction best equipped to carry out the desired community objective. In view of these manifest advantages, the continued expansion of grant programs in the rapidly-growing West appears all but certain.

Western Digest

Banking Developments

At year-end, Twelfth District weekly reporting banks had on their books $32,314 million in outstanding bank credit—up $452 million from the end-November figure. But December's 1.4-percent increase failed to match the 2.4-percent gain recorded in the comparable month of 1963, when security and loan portfolios both increased at a faster pace. . . . Outstanding loans increased $410 million in December, reflecting both mid-month tax-connected borrowing and strength throughout the month in credit demand from the business sector, including sales finance and other nonbank financial institutions. Real estate loans, on the other hand, showed only a negligible gain during the month. . . . Demand deposits adjusted increased 1.1 percent in December, for a somewhat smaller gain than in the year-ago month. But total time and savings deposits increased 3.1 percent ($556 million) as banks received unusually large seasonal deposits from states and political subdivisions. A $115-million gain in savings deposits, which reflected year-end crediting of interest, was greater than a year earlier and thus also helped to account for the year-end strength in the time-and-savings category.

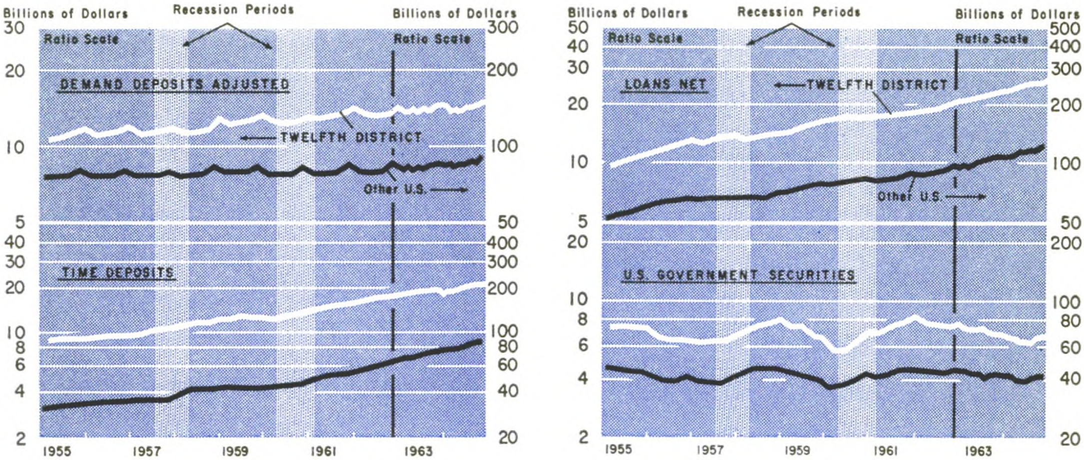
Employment and Unemployment

Total employment increased 0.8 percent in California and 0.4 percent in Washington in December, on the strength of gains in both the farm and nonfarm sectors. In the nation as a whole, a drop in farm employment partly offset an increase in the nonfarm sector, and thereby held the gain in total employment to 0.2 percent. . . . Jobless rates in the region declined substantially in December, to 6.0 percent in California and to 5.4 percent in Washington. The national unemployment rate, although somewhat lower, actually increased slightly during the month, to 5.0 percent. (All data seasonally adjusted.)

Storm Damage

Three weeks of stormy weather with heavy rainfall caused flooding and extensive damage in southern Washington, Oregon, and northern California during late December and early January. Roads and railway lines were washed out or blocked by landslides in some areas, and many bridges were destroyed by the force of flood waters carrying logs, building wreckage, and other debris. . . . Flood damage was especially severe along the Willamette River in Oregon and along the Eel and Russian Rivers in California. Total damage ran into several hundred million dollars, according to Army Corps of Engineers estimates. . . . The lumber industry suffered serious losses. Lumber mills in Oregon and Washington were unable to resume operations until late January, and mills in northern California (with 4,000 lumbermen out of work) anticipated an even longer delay. A single redwood mill in that region reported losing 18 million board-feet of logs and 22 million board-feet of cut lumber in the washout.

Condition Items of All Member Banks — Twelfth District and Other U. S.



Source: Federal Reserve Bank of San Francisco. (End-of-quarter data shown through 1962, and end-of-month data thereafter; data not adjusted or seasonal variation.)

BANKING AND CREDIT STATISTICS AND BUSINESS INDEXES—TWELFTH DISTRICT[1]

(Indexes: 1957-1959 = 100. Dollar amounts in millions of dollars)

Year and Month	Condition items of all member banks[2] Seasonally Adjusted				Bank debits Index 31 cities[5], [6]	Bank rates on short-term business loans[7], [8]	Total nonagri-cultural employ-ment	Dep't. store sales (value)[6]	Industrial production (physical volume)[6]		
	Loans and discounts[3]	U.S. Gov't. securities	Demand deposits adjusted[4]	Total time deposits					Lumber	Refined[8] Petroleum	Steel[8]
1951	7,751	6,370	9,512	6,713	57	3.66	80	68	99	87	97
1952	8,703	6,468	10,052	7,498	59	3.95	84	73	101	90	92
1953	9,090	6,577	10,129	7,978	69	4.14	86	74	102	95	105
1954	9,264	7,833	10,194	8,680	71	4.09	85	74	101	92	85
1955	10,827	7,162	11,408	9,130	80	4.10	90	82	107	96	102
1956	12,295	6,295	11,580	9,413	88	4.50	95	91	104	100	109
1957	12,845	6,468	11,351	10,572	94	4.97	98	93	93	103	114
1958	13,441	7,870	12,460	12,099	96	4.88	98	98	98	96	94
1959	15,908	6,495	12,811	12,465	109	5.36	104	109	109	101	92
1960	16,628	6,764	12,486	13,047	117	5.62	106	110	98	104	102
1961	17,839	8,002	13,676	15,146	125	5.46	108	115	95	108	111
1962	20,344	7,336	13,836	17,144	141	5.50	113	123	98	111	100
1963	22,915	6,651	14,179	18,942	157	...	117	129	103	112	117
1964	25,561	6,522	14,505	21,172	169	...	...	...	...	...	...
1963											
December	22,915	6,651	14,179	18,942	167	5.47	118	136	112	110	107
1964											
January	23,256	6,575	14,332	19,342	163	...	119	135	115	111	110
February	23,544	6,832	14,222	19,520	167	...	119	137	114	115	117
March	23,763	6,893	14,287	19,685	165	5.47	119	133	114	113	149
April	23,953	6,559	14,243	19,773	169	...	119	134	102	111	140
May	24,102	6,541	14,170	19,813	166	...	119	139	106	112	139
June	24,394	6,489	14,347	19,876	167	5.46	119	137	105	114	131*p*
July	24,836	6,215	14,369	20,152	166	...	119	141	113	115	121*p*
August	24,865	6,170	14,362	20,195	175	...	120	143	107	118	121*p*
September	25,257	6,507	14,674	20,452	166	5.51	120	137	108	121	129*p*
October	25,140	6,473	14,573	20,602	173	...	121	139	111	117	132*p*
November	25,339	6,668	14,545	20,792	178	...	121	151	...	113	149*p*
December	25,561	6,522	14,505	21,172	167	5.48	122*p*	...	...	...	140*p*

[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, U.S. Bureau of Mines; steel, U.S. Department of Commerce and American Iron and Steel Institute; nonagricultural employment, U.S. Bureau of Labor Statistics and cooperating state agencies. [2] Figures as of last Wednesday in year or month. [3] Total loans, less valuation reserves, and adjusted to exclude interbank loans. [4] Total demand deposits less U.S. Government deposits and interbank deposits, and less cash items in process of collections. [5] Debits to demand deposits of individuals, partnerships, and corporations and states and political subdivisions. Debits to total deposits except interbank prior 1942. [6] Daily average. [7] Average rates on loans made in five major cities, weighted by loan size category. [8] Not adjusted for seasonal variation. *p*—Preliminary. *r*—Revised.