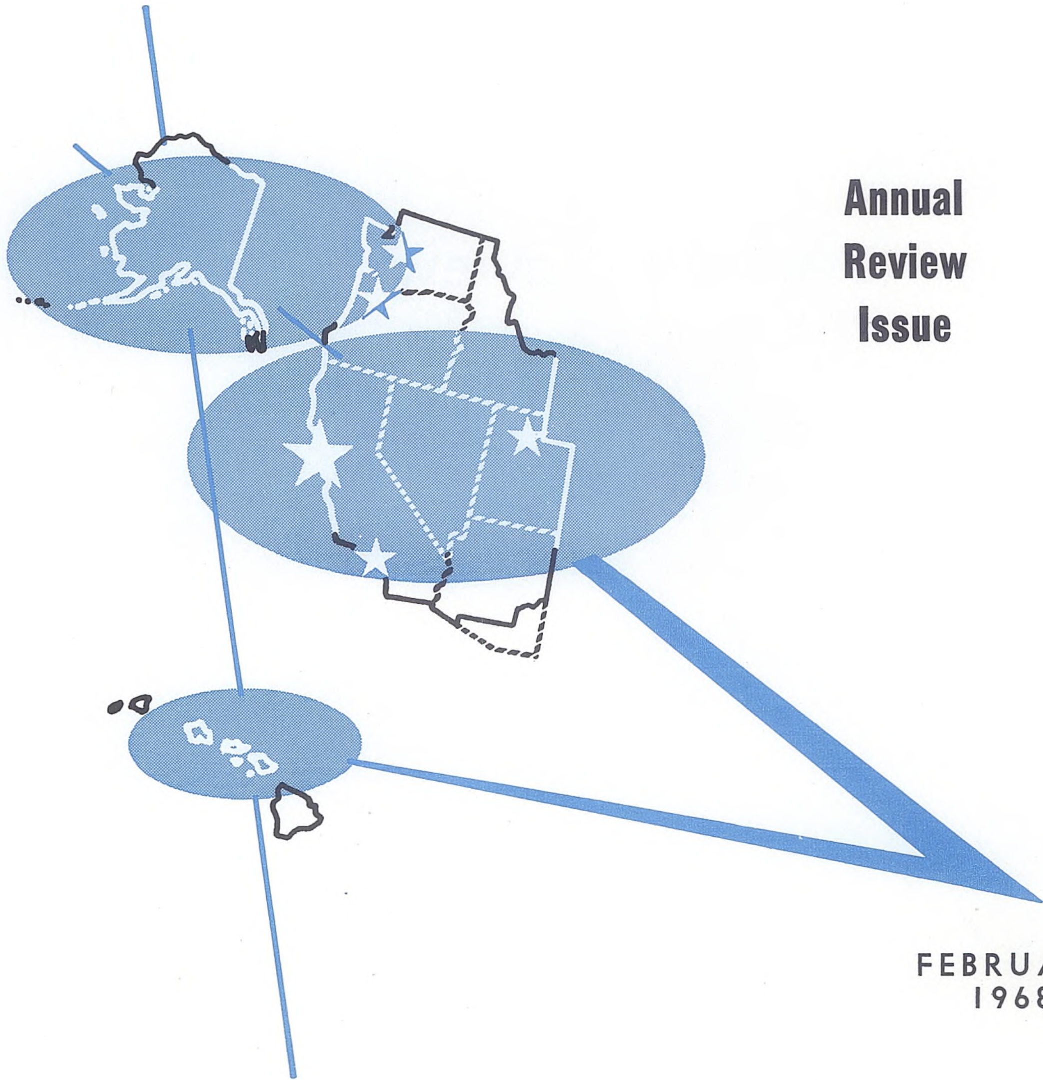
FEDERAL RESERVE BANK OF SAN FRANCISCO

MONTHLY REVIEW



Annual Review Issue

FEBRUARY
1968

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Annual Review 1967

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Not Quite So Great
Not Quite Full Circle
Pounds, Dollars — and Problems
Financing Patterns
Banking '67 Style
Outpacing the Nation
Calmer Sailing
Catalog of Expansion

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Not Quite So Great

Nineteen sixty-seven was not one of the all-time-great years. The nation had more than its quota of political problems, both at home and abroad, and its economic performance left something to be desired in several different respects. The economy recorded a measure of growth and a high level of employment, but it failed to keep its costs and prices in line and—especially after the November devaluation of the British pound—this failure created ominous implications for the nation's international payments position.

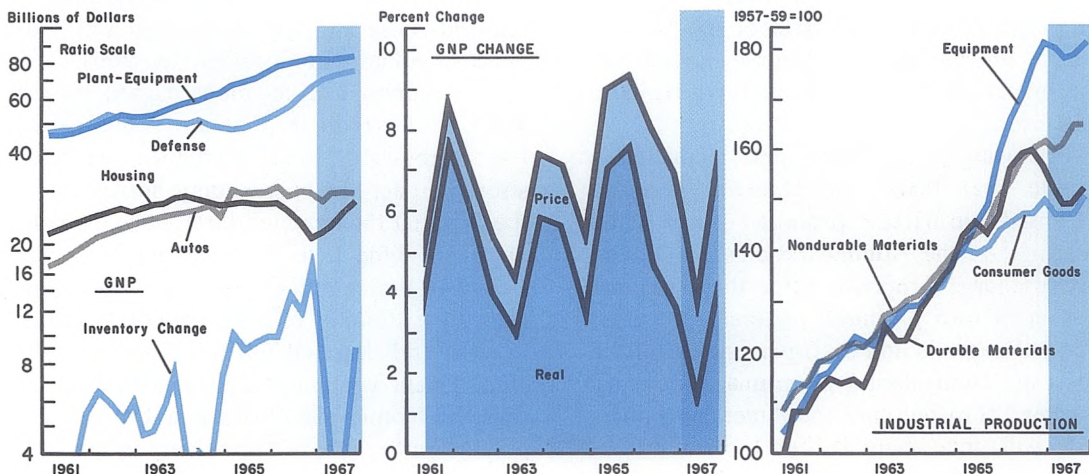
Total output of goods and services rose 5½ percent during the year to $785 billion. In real terms, after adjustment for rising prices, the gain amounted to only 2½ percent, the smallest since the 1961 recession. Industrial production meanwhile moved sideways most of the year, averaging out at 58 percent above the 1957-59 base. (Coincidentally, production in the Common Market bloc followed the same general pattern during 1967.)

Shifts in the economy

By year-end, the 80 million workers in the national economy were producing at an $800-billion annual rate. (GNP at the beginning of the decade was only $500 billion.) Both producers and consumers, however, underwent a shift in attitudes over the course of the year. When the economy stopped growing in real terms in early 1967, they were beset by fears of recession; when price increases took hold in the more ebullient atmosphere of late '67, they became increasingly concerned over inflation. The psychological atmosphere, in a word, shifted from fear of recession to fear of boom between early and late year.

The late-year expansion developed rather naturally out of the earlier pause. There was no major accumulation of deferred demands,

Expansion of defense sector, stability of fixed-investment spending, and wild swings in inventories—along with price upsurge—mark '67 economy



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

of the type that build up during a thoroughgoing recession to create the conditions for a consequent boom. Even at year-end there was little evidence of excess demand driving buyers to scramble frantically for goods. But just the same, business activity was definitely advancing, skilled labor supplies were taut, recession fears were forgotten, and inflation fears instead were dominant, reinforced as they were by a large Federal deficit and numerous price increases.

Shifts in policy

Public policy during this difficult year was called upon to dampen the sharp swings of business activity and business psychology—that is, to ensure that neither recession nor runaway inflation would be realized. Undoubtedly, the stimulus provided by a large budget deficit and an easier monetary policy swamped the incipient downturn of early '67.

By late year, however, some shifting of gears became necessary to contain the threat of inflation, and the problem was of course compounded by the British devaluation and the consequent attack on the dollar in the world's financial markets. Congress adjourned without acting on the Administration's proposals to reduce the size of the Federal deficit, but the Federal Reserve moved into the breach with several credit-tightening measures.

Following a prolonged and inconclusive debate over taxes, the House Ways and Means Committee promised early 1968 hearings on the Administration's 10-percent tax-surcharge proposal, after the Administration in turn promised a 2-percent cut in Federal payrolls and a 10-percent cut in the costs of "controllable" programs. (Secretary Fowler: "I'm not sure the American housewife will understand it, but I certainly believe that the devaluation of the British pound makes a tax increase imperative.") The increase in taxes and the concomitant decrease in Federal spending would be designed to reduce the deficit and thereby reduce inflationary demand. Accomplishment of those goals should help make U.S. goods more competitive in world markets and imports less attractive to U.S. buyers, and thus should stimulate the expansion of the trade surplus, so that it can better provide the necessary support for U.S. military and economic activities abroad.

Vietnam impact

Military spending during 1967 provided much of the pressure on the domestic economy as well as on the U.S. international position. Defense spending rose 20 percent during the year to $75 billion—the sharpest gain since Korean War days. Federal spending for nondefense goods and services meanwhile rose about 5 percent to $17 billion—the smallest gain of any recent year except 1966. (State-local government spending as usual rose about 10 percent, to $86 billion.) Yet by year-end the growth of defense outlays began to slow down, presaged by a yearlong stability of military contract awards, and some nondefense sectors were sharply reduced, offsetting increases voted by Congress in military and civilian payrolls.

The economic dislocations caused by the 1965 escalation in Vietnam continued in force throughout 1967. Vietnam's continued strong impact on the economy derived from the fact that the size and duration of the conflict were difficult to measure, and from the fact that the military spending surge reinforced the stimulus of the broadest tax cut in history, and thus fell full force upon a full-employment economy. The development of sharp economic distortions is not at all surprising; rather what is surprising is the lack of greater distortions and much more rapid

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

inflation in the wake of such a large and uncontrollable historical event. But the economy's ability to handle this event has been helped by the strength of underlying long-term growth factors, especially the recent sharp gains in the nation's labor force and in its industrial capacity.

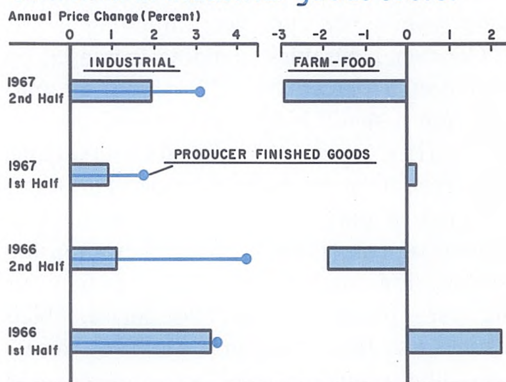
Business impact

Most of the gain in capacity stemmed from the several preceding years' boom in business investment, since that boom definitely tapered off in 1967. Business capital spending rose only about 3 percent to $82 billion—the smallest gain of the decade—as a decline in industrial building offset most of the strong increase in equipment purchases.

Businessmen opened the year with expectations of a somewhat higher level of plant-equipment spending, but they were induced to lower their sights as industrial production leveled off and as capacity utilization rates fell. They were also influenced by the very high level of borrowing costs, with rates approaching 7 percent on some corporate bonds. Nonetheless, corporations were willing, even anxious, to take advantage of long-term financing possibilities. More corporate issues were issued in the first three-quarters of the year than in the entire preceding year, partly because of the cumulative financial effects of the preceding investment boom, and partly because of the attempt to rebuild liquidity in the face of a possible shortage of funds in the uncertain future.

In the inventory sector, purchasing agents added only about $5 billion to business stocks during 1967—about $8 billion below the unsustainable stockbuilding pace achieved in the preceding year. In fact, an $18-billion turnaround occurred between late '66 and mid '67, as businessmen (especially retail merchants) failed to increase

Rise in wholesale-price index centered in industrial-goods sector



their stocks and thereby imparted the decidedly slack tone to early-year business activity. A moderate buildup then took place in the latter part of 1967.

Surprisingly, inventories in durable manufacturing were still relatively high at year-end. Defense goods, which require a long lead-time in production, accounted for a substantial part of the rise in factory stocks. Because of this and other factors, the inventory-sales ratio in manufacturing rose from a high 1.70 in late 1966 to an even higher level of 1.75 in late 1967. And at year-end, purchasing agents again were stockpiling heavily—especially in steel, because of the industry's mid-'68 labor contract deadline.

Consumer impact

Consumers responded to the rather uncertain business atmosphere during 1967 with an appropriately cautious performance. Although personal income rose by about 7 percent to $626 billion, consumer spending rose at a slower pace and the personal saving rate thus jumped to 7 percent—the highest figure in a decade and sharply above the average 1960-66 rate of about 5½ percent. Consumers were also concerned about the growing bite of Federal and state-local personal

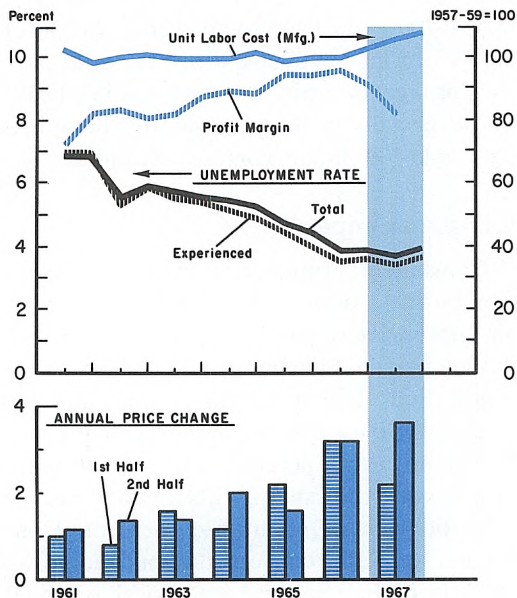
Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

taxes (plus social security), which increased from 14.7 to 16.3 percent of personal income within only a two-year time span.

Consumer durables spending increased by a modest 3 percent to $72 billion, as auto sales fell a shade below the level of the two preceding years while furniture-appliance sales rose at a rather brisk pace. The latter reflected in part the sharp improvement in residential construction. While new housing construction totaled only $24½ billion for the year—the same as the 1966 figure, which in turn was the worst since the 1961 recession—the spending pace at year-end was one-third ahead of the dismal pace of late '66.

The '68 auto market was difficult to measure because of strike activity at the start of the model year; the '67 model year, however, was the first since 1961 to register a decline. Sales of domestic models dropped to 7.9 million units from the '66 level of 8.5 million units, but sales of foreign cars jumped 17 percent to 750,000 units. The contrast was strikingly reminiscent of developments a decade ago, since foreign cars in both instances sharply increased their market penetration to 9 percent of total U.S. sales. Now as then, Detroit producers showed their preference for higher-priced models; cars priced over $2,500 increased from one-third to two-thirds of total domestic production between 1961 and 1967.

Cost-push inflation reflects drop in profits and rise in labor costs



Labor, costs, and prices

The uncertainty as well as the strong undertone exhibited by consumer markets reflected developments in the nation's labor market. Civilian employment drifted downward during the early '67 slowdown, but for the year as a whole it rose 2 percent to 74 million. Unemployment averaged about 3.8 percent, the same as in the preceding year. The jobless rate for unskilled workers was several times that figure—and as the midsummer riots revealed, the rate of unemployment and underemployment reached 35 percent in some ghetto areas. At the same time, skilled workers remained very much in demand; the jobless rate for the family-breadwinner category was below 2 percent for the second consecutive year.

The early-year slack in business activity showed up in declining job opportunities in construction and durable manufacturing, and also in a drop in the average factory workweek. But a strong market for skilled labor led unions to demand (and to get) stiff increases in hourly wages. One result was the 7-percent increase in personal income, matching the 1966 increase. But after adjustment for increases in population, prices, and taxes, the end-result was only a 3-percent gain in real take-home pay, the smallest gain of the last four years.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Price pressures showed up in a 3-percent increase (for the second straight year) in consumer prices, to a level 16 percent above the 1957-59 base period. Pressures also showed up in the wholesale-price index, which actually remained stable at about 6 percent above the 1957-59 base, but only because of price weakness in farm and food products and crude industrial materials. Wholesale prices in the crucial industrial sector—for both materials and finished products—increased sharply after midyear because of the over-all improvement in the demand outlook and because of rising labor and other costs in critical manufacturing areas.

Higher manufacturing costs were associated with higher wages and a falling rate of capacity utilization, along with a related slowdown in productivity growth. Output per man-hour rose only 2 percent, or at about half the average 1960-66 pace. Unit labor costs in manufacturing, after remaining stable throughout the earlier part of the decade because of productivity gains, thus jumped 8 percent between mid-1966 and late 1967. And the upsurge in cost pressures, together with the slowdown in total demand, cut sharply into corporate profit margins after a six-year-long period of expanding profits.

In this area of cost control, 1967 unhappily repeated the experience of 1966. During the prolonged earlier period of stable costs, the pressure of output on capacity grew slowly, the jobless rate declined slowly, productivity increased sharply—and total employee compensation advanced fairly slowly under the pressure of industrial slack and Washington guideposts. But during the past two years, the labor market became increasingly tight, wage rates grew at an accelerated pace, productivity grew at a decelerated pace—and the usual increase in total labor costs went along with a drop in corporate output.

The London *Economist* best summed it up: "It is not, in any sense, a comfortable situation—concern about the dollar abroad, wages and prices rising at home faster than the United States is used to, interest rates at record levels in the face of an easy monetary policy, a huge deficit on the budget—and yet no evidence of excess demand except what can be produced by forecasts. The English disease? Hardly. But it is the most disconcerting time for this huge, successful economy in at least ten years."

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Not Quite Full Circle

In 1967, both monetary and fiscal policy were highly expansive. The Treasury ran the largest deficit of any calendar year since World War II, and the Federal Reserve supplied reserves to the banking system in the largest volume since 1945. But in spite of the expansive nature of policy, the financial markets had problems in absorbing the record amounts of corporate and municipal securities that were marketed during the year, and long-term interest rates rose to heights not seen since the Reconstruction Era.

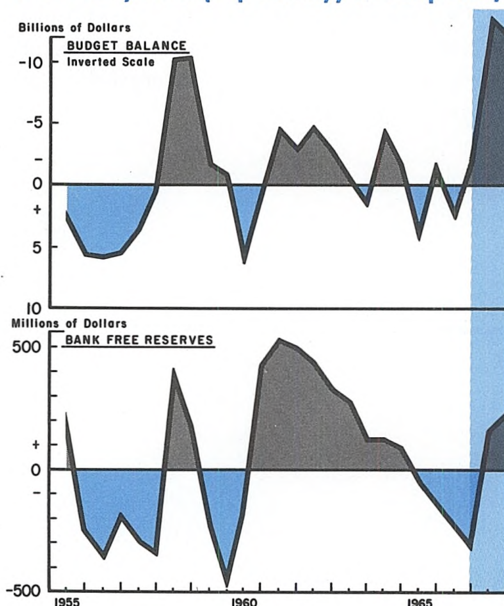
Income disappointing; outgo rising

The Federal budget underwent severe pressure from both sides during 1967. Revenues for the first half of fiscal 1968 fell below the estimates made in January, while expenditures (chiefly for defense) rose rapidly. The resulting deficit for calendar 1967 was the largest since 1945—$12.6 billion on the national-income-accounts basis, which measures the economic impact of Federal purchases of goods and services along with Federal transfers and grants-in-aid.

The Treasury borrowed a net total of about $5.8 billion from the public during the year, through the sale of its own securities and participation certificates in pooled Federal loans. The cash needs of the Treasury were concentrated in the second half of the year, reflecting the "feast-famine" cycle of revenue inflows. Consequently, a very sharp turnaround occurred between the second and third quarters of the year as the Treasury switched from being a net repayer of debt to a net borrower.

In the spring, the Administration restored the 7-percent investment-tax credit that had been suspended the preceding November, and it released about $2.1 billion of various construction and mortgage assistance funds that had similarly been frozen in late 1966. However, as the Federal deficit soared, the need for restrictiveness became apparent, and the President proposed a 6-percent (later raised to 10-percent) surcharge on personal and corporate income-tax liabilities. Yet, by year-end, Congress had failed to take any action on the proposal.

Economy stimulated by easy monetary and (especially) fiscal policy



Monetary policy . . . and results

Nineteen sixty-seven was one of those years which delight teachers of money and banking looking for concrete examples of policy change, since all three of the instruments of general monetary control were utilized in the course of the year. In March, reserve requirements against savings deposits and time deposits of up to $5 million were reduced from 4 percent to 3 percent, the bottom of the discretionary range of reserve requirements against such deposits. In April,

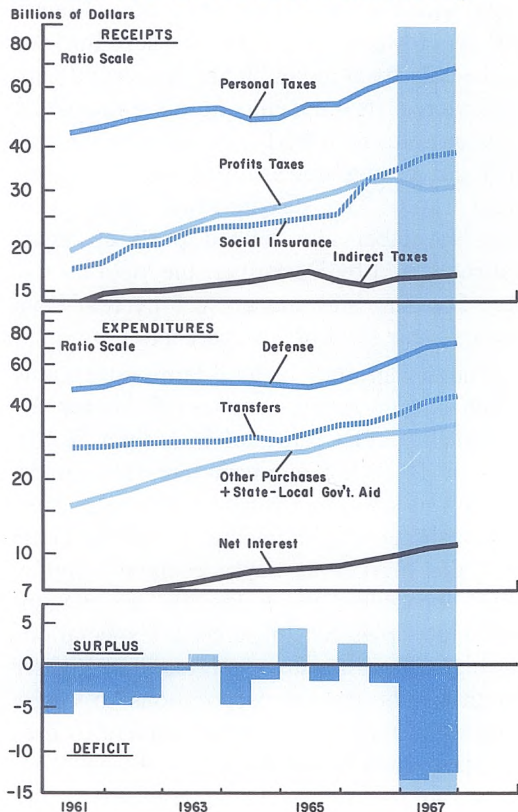
Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

the discount rate on advances to member banks was lowered from 4½ to 4 percent. Both of these actions followed the shift toward easier monetary conditions that was initiated the preceding November.

Additionally, the Federal Reserve in the first quarter increased its holdings of U.S. Government securities by over $¼ billion through open-market operations. The reserve position of the member banks moved from small net borrowed reserves in January and February to net free reserves of $236 million in March. The member banks maintained a comfortable cushion of net free reserves through the remainder of the year, although that cushion narrowed somewhat in the fourth quarter.

In November, immediately upon the heels of the British devaluation, the discount rate was put back up to 4½ percent. The increase was directly related to the defense of the dollar in international financial markets, but this action also served to bring the discount rate into line with domestic money market rates. And by year's end, "Fed-watchers" detected evidence of a change in monetary policy away from the prevailing degree of ease. In the last week of December the Board of Governors announced an increase of ½ of 1 percent in reserve requirements against demand deposits in excess of $5 million, to take effect in January 1968.

The monetary expansion of 1967 owed much to the open-market operations of the Federal Reserve: the securities holdings of the System Open Market Account increased by over $5½ billion during the year. This, the largest net open-market purchase of securities for any year since 1945, was accompanied by a record expansion in bank credit and in the money supply. Total bank credit increased by 11 percent, while the money supply expanded at a 6½-percent average rate. The expansion of bank credit also owed something to the very substantial increase in



commercial bank time-and-savings deposits, which grew sharply by 16 percent. The credit expansion, incidentally, centered in securities rather than loans; when loan demand slackened in response to the corporate switch to capital-market financing, the banking system became an active underwriter of government securities, particularly municipal issues.

Interest rates: up again

Interest rates moved up vigorously in the second half of 1967, after trending downward during much of the first half. Short-term rates, as typified by the market yield on 91-day Treasury bills, fell by about 1½ percentage points from December 1966

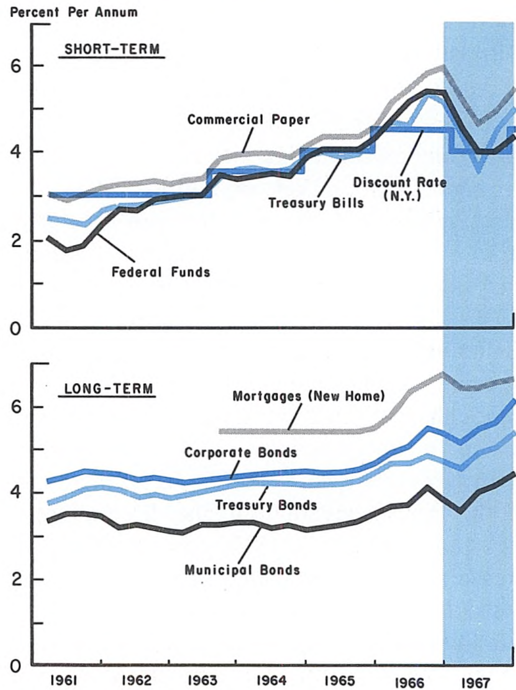
Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

through the following June, reflecting the Treasury's redemption of tax-anticipation bills and the increasing ease of monetary policy. However, when the Treasury borrowed heavily from the public in the second half, it centered its financing in tax-anticipation bills or notes with fairly short maturities, and this put strong upward pressure on short-term rates. The discount-rate increase in mid-November also helped push up interest rates, and by December, the yield on 91-day Treasury bills was up to 5 percent from the midyear level of 3½ percent.

The turnaround in long-term rates came much sooner in the year—in February for top-quality corporate and municipal bonds, and in March for long-term Treasury bonds. There was steady pressure on long-term rates as corporate and municipal securities came into the market in unprecedented volume, with corporates increasing by 36 percent and municipals by 26 percent. Expectations of high interest rates and fears of tighter credit conditions led corporations to desire long-term borrowing and led lenders to prefer short-term investments.

The effect of these forces is shown in the changing shape of the yield curve for U.S. Government obligations. At the end of December, long-term yields had receded some-

Interest rates reverse earlier drop and surge upward again in late '67



what from their highest levels but were still well above the levels reached at the time of the "crunch" in the summer of 1966. However, short-term yields were still below 1966 peaks.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Pounds, Dollars—and Problems

The year was marked by several major developments in the international economy. On the plus side, international monetary authorities reached agreements on widespread tariff reductions and on the joint international creation of a new monetary reserve asset. On the other hand, the pound sterling was devalued, and this was followed by a speculative attack on the U.S. dollar which was then repulsed by the Gold Pool. In addition, the U.S. balance-of-payments deficit worsened considerably, leading, at the beginning of the new year, to the imposition of mandatory controls over U.S. direct investment abroad, tighter guidelines under the Voluntary Foreign Credit Restraint Program, and proposals for legislation to reduce the deficit further.

New asset . . . and trade

After four years of intensive study and discussion, members of the International Monetary Fund met at Rio de Janeiro in September and reached agreement on a method for supplementing world gold and foreign-exchange reserves in accordance with long-range international liquidity needs. The new reserve asset is in the form of a Special Drawing Right (SDR) in the Fund, available to all members of the Fund, and is to be allocated among members in proportion to their IMF quotas. SDRs will be denominated in terms of gold, although not convertible into gold, and their creation will require approval by 85 percent of total IMF votes.

At the end of June, the U.S. and 52 other governments concluded the sixth round of GATT trade negotiations — the Kennedy Round — with an agreement designed to facilitate the liberalization of world trade. In all, tariff concessions were made by 37 participants who account for some 75 percent of world trade.

Substantial tariff reductions were negotiated on the $40-billion trade in industrial products, amounting to an estimated 35-percent reduction over the next five years. U.S. import duties are to be halved on a wide range of industrial goods, and reductions on other items ranged from 30 to 50 percent. Average tariff reductions on industrial goods by this country's major trading partners will amount to about 35 percent by the European Economic Community, 30 percent by Japan, 24 percent by Canada, and 38 percent by the United Kingdom.

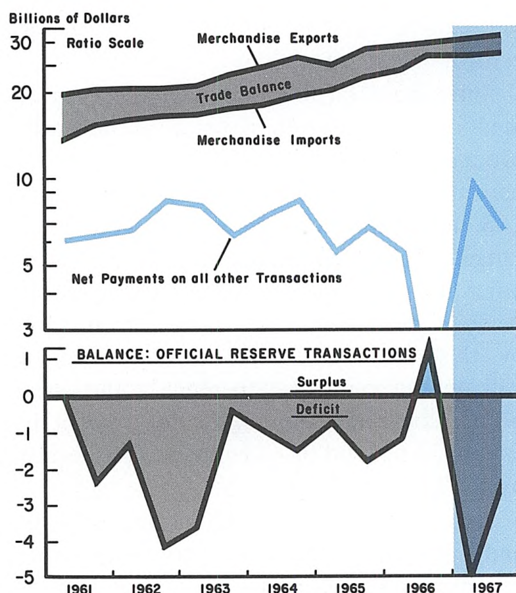
Agreement was also reached on maximum and minimum world wheat prices and on a program of aid to developing countries which will involve 4.5 million metric tons of grain annually. Chemical products, treated in a separate agreement, were accorded partial and unconditional tariff reductions immediately by the EEC and the U.K., while the U.S. is to effect full tariff cuts on a limited list of chemical products. Additional European tariff cuts are to be conditional upon the passage of legislation abolishing the American-selling-price system of valuation.

Background to devaluation

In November, the British government devalued the pound from $2.80 to $2.40 despite strong support from the U.S. and other countries in defense of the former parity. Ever since the last devaluation in 1949, the pound had experienced periodic fainting spells, due primarily to speculation centering on sporadic balance-of-payments weaknesses and continuing reserve deficiencies—and to domestic circumstances that seemed to place greater emphasis on consumption than on productivity and economic growth.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

U. S. payments deficit worsens even before late-year financial crisis



The devaluation came only after determined efforts had been made to correct the persistent disequilibrium in Britain's external accounts. These efforts centered around the restraint of demand for the two-fold purpose of holding down imports and of releasing goods for export. To accomplish this, the Government adopted a program of severe monetary and fiscal restraint and imposed an absolute standstill on prices and incomes during the last half of 1966.

As 1967 began, these measures appeared to be taking hold. A large fourth-quarter surplus had developed in the basic balance on current and long-term capital account, and this development (with the continuing support of foreign central banks and international financial institutions) dampened speculative pressure against the pound. Basic weaknesses in the British economy—overfull employment, unsustainably high consumption levels, and the concomitant upsurge in imports and diversion of goods from export to domestic markets—seemed well on the way to solution.

As 1967 unfolded, however, the realization of these hopes receded further and further into the future. After the wage-price freeze was lifted in January, wage rates began rising again, and by September were more than 3½ percent above the January level. Meanwhile, the trade deficit reappeared. Imports, already bolstered by the end of a seamen's strike and the lifting of an import surcharge, increased even more rapidly than expected. And exports failed to provide adequate balance-of-payments support, partly because of the slowdown in economic activity elsewhere in Western Europe —particularly in West Germany, a major market for British goods.

The outbreak of war in the Middle East interposed further hurdles in Britain's difficult path towards balance-of-payments equilibrium. With the Arab oil embargo and the closing of the Suez Canal, oil had to be shipped to Britain over longer distances, with payment in non-sterling currencies (and in some cases at premium shipping rates), thus placing a further drain on British reserves. During the summer months, too, British exports suffered from the dock strikes in Liverpool and London, and also from the Arab boycott on British goods.

Thus, a combination of unfavorable factors, both at home and abroad, contributed to a severe weakening of Britain's international position. Sharply rising trade deficits in August, September, and October undermined confidence in the pound and touched off a massive speculative capital outflow.

Devaluation and after

At that point, if devaluation were to be avoided, Britain had no choice but to deflate its economy severely, to impose various controls to relieve presure on the pound, and also to liquidate its foreign assets and borrow

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

heavily from abroad to provide a transitional cushion of reserves. The alternative to maintaining the current overvalued $2.80 parity was to seek an improvement in competitive position through devaluation, scaled so that it would not be matched by other major countries.

The case for devaluation was bolstered by the presumed political impossibility of achieving adequate internal discipline without this crisis signal, and also by the presumption that devaluation was a necessary step to membership in the European Economic Community. In any case, Britain opted for devaluation.

The Government might well have preferred the greater competitive advantage that would have accompanied a deeper devaluation, but it recognized that a greater reduction in the parity of the pound might jeopardize the trading interests of other major countries and lead to offsetting devaluations in the EEC and elsewhere in the industrial world.

The new parity is backed by foreign credits totalling some $3 billion, including a $1.4-billion standby arrangement with the International Monetary Fund. These credits, of course, are for the purpose of helping Britain maintain the new parity while fundamental adjustments are made in the domestic economy. In order to safeguard the external benefits of the devaluation and to create domestic conditions more favorable to real economic growth and higher levels of real income based on rising productivity and output, the British government undertook a stringent stabilization program in the post-devaluation period.

Initially, the Bank of England raised its discount rate, from 6½ to 8 percent, and requested the commercial banks to restrain their lending. In addition, loan-payment requirements on installment purchases of automobiles were raised and the maximum repayment period reduced.

The second stage of the stabilization program followed in mid-January. Planned public expenditures are to be reduced by $720 million in 1968-69 and by almost $1 billion in 1969-70. (These reductions are in addition to those announced at the time of devaluation.) Cuts are scheduled immediately in education, health, welfare, and road and housing construction. Reductions in defense expenditures will be effective later; these include withdrawal of virtually all British forces "East of Suez," cancellation of an order for U.S. military planes, and the phasing out of the Royal Navy's aircraft carriers.

The success of devaluation in restoring equilibrium to the British balance of payments will depend very largely on the willingness of Britain — and particularly the British public — to accept the costs which adjustment will necessarily impose. Prices of imports, including food, are rising, while increases in incomes must be restrained in the interest of freeing goods for export and of preserving the export price advantage potentially conferred by the devaluation.

Not all this potential has been captured, however; there has been some tendency for prices on certain export products to rise in a manner offsetting the devaluation benefits. Nevertheless, if the British economy can be restructured and the pattern of spending altered to insure export-led economic growth, both Britain and its currency should continue to have an important place in the world economy.

The U.S. problem . . .

The devaluation of the pound accentuated the continuing U.S. balance-of-payments problem. First, the British defensive actions, involving liquidation of investments in this country, contributed to a sizeable outflow of dollars. Second, the U.S. also recorded some further outflows and some trimming of in-

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

flows that would otherwise have taken place. Third, the overgeneralized loss of confidence in reserve currencies caused the dollar as well as the pound to come under sharp speculative attack.

Yet the U.S., in cooperation with other members of the Gold Pool, succeeded in maintaining the established price of gold and in stabilizing the international payments mechanism in the wake of the British devaluation. These operations involved heavy gold sales by the Gold Pool.

December's decline in the U.S. gold stock —$900 million—dwarfed the $74-million decline of November and greatly exceeded the (relatively light) $196-million loss of the first ten months of the year. (U.S. gold losses for the year as a whole have been exceeded in several recent years.)

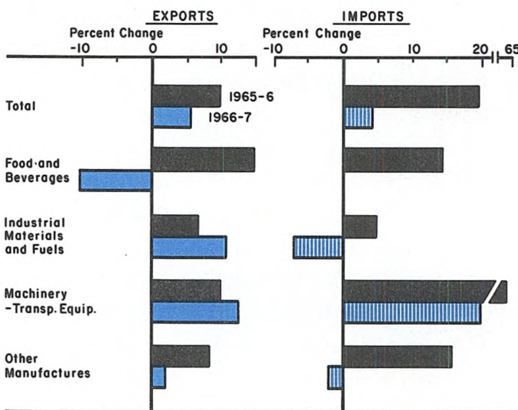
Action was also taken to strengthen the dollar's defenses against future speculative attacks. Federal Reserve swap arrangements with foreign central banks were increased from $5.0 to $6.8 billion. The narrowing of the margin of "free gold" reserves served to emphasize the need to remove the gold-certificate reserve requirement for Federal Reserve notes, and thus to free some $10.6 billion of gold currently held as "backing" for the note issue. Thus, in January, Congress began to consider legislation designed to remove the gold backing.

Behind this turmoil was a distinct worsening of the balance-of-payments deficit. On the official-reserve-transaction basis, the U.S. payments position shifted from a slight surplus in 1966 to a $2.9-billion annual deficit in January-September 1967 — and it then deteriorated sharply in the final months of the year. The deficit was in the neighborhood of $3.5 billion for the year as a whole.

Part of the sharp fourth-quarter deterioration was due to special factors. One such factor was the liquidation of Britain's government-held portfolio of U.S. stocks and bonds, which involved a shift of some $500 million from long-term to short-term U.S. liabilities, and thus a worsening of the deficit by that amount. Another factor was a decline in foreign official purchases of U.S. securities with maturities of over one year. In previous periods such purchases, counting as capital inflows, helped to reduce the deficit.

Of greater basic significance, however, was the fourth-quarter weakening of the trade surplus — especially in December, when the export surplus amounted to only $79 million (seasonally adjusted), the smallest monthly figure in nearly three years. For the year as a whole, the trade surplus totalled $4.1 billion compared with $3.8 billion the previous year. And other deficit factors included increased foreign-exchange expenditures in Vietnam, larger outflows of private capital, and a substantially greater deficit on travel account.

Trade balance suffers, with exports as well as imports rising sluggishly



. . . and the U.S. program

To meet the worsening balance-of-payments situation and to forestall any speculative attack which might be triggered by the disappointing fourth-quarter results, the President announced, at the beginning of the

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

new year, a comprehensive program to improve the U.S. balance of payments in 1968 by an estimated $3 billion. All sectors of the economy were called upon to help carry out this program, although its major impact will be felt by the investment and tourist sectors.

Mandatory controls were imposed on U.S. direct investment abroad, replacing the direct-investment targets previously announced for 1968. New direct-investment outflows to continental Western European countries and to certain others not heavily dependent on U.S. capital are to be halted in 1968. In other developed countries, net new U.S. direct investment outflows are to be limited to 65 percent of the 1965-66 average, while in developing countries such investment outflows will be permitted up to 110 percent of the 1965-66 average. This part of the program is designed to contribute $1 billion toward improving the balance of payments in 1968.

The Federal Reserve, with responsibility for the voluntary credit restraint program, set lower guideline ceilings for financial institutions, and requested banks not to re-lend long-term bank credits repaid by developed countries of continental Europe and to reduce by 40 percent the outstanding short-term credits to those countries. The new regulations also included a request for a 5-percent cut in the holdings of foreign assets by nonbank financial institutions. With the cooperation of banks and other financial institutions, this part of the program is expected to contribute some $500 million to improving the deficit during the current year.

The program also calls upon U.S. citizens to defer nonessential travel outside the Western Hemisphere during the next two years. Moreover, legislation has been introduced to tax the dollars spent abroad by U.S. travelers, above a certain daily minimum. This part of the program is expected to result in a substantial improvement in the travel account.

A $500-million reduction in the net payments impact of government expenditures abroad is also envisioned by the program. Foreign purchases of long-term U.S. securities and defense equipment are to be encouraged as offsets to the foreign-exchange costs of maintaining U.S. troops overseas. Efforts are also to be made to find ways to reduce the foreign-exchange impact of personal spending abroad by military personnel, and to curtail the number of U.S. civilian personnel assigned outside the U.S.

Longer-range measures include a five-year export-promotion program to be carried out under the direction of the Department of Commerce, and improved export insurance and export-financing guarantees through the Export-Import Bank. Efforts are also to be made to reduce non-tariff barriers to world trade; hopefully, this would increase the U.S. trade surplus by $500 million during the current year. In addition, efforts are to be made to encourage foreign investment and travel in the U.S.

Analyzing these problems in its recent annual report, the Council of Economic Advisers concluded: "There is a clear need for a new demonstration of the flexibility" of the international payments system. No longer can the world rely upon continued deficits in the U.S. balance of payments for the creation of adequate reserves. At home, there will be needed (among other things) "a resolute and continuing attack on inflationary pressures." Abroad, there will be needed "the cooperation of all countries, especially those with persistent surpluses, in bringing about better equilibrium."

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Financing Patterns

The total amount of funds raised through the financial markets reached a new peak of $75 billion in 1967. Nevertheless, the dollar increase over the previous year was smaller than any other increase since the beginning of the decade. Moreover, total private borrowing actually declined during the year, as borrowing demands were concentrated in the government sector, especially the state-local government sector.

In 1967, commercial banks and other financial institutions emphasized their dominant place on the supply side of the market, and households backed away from the glittering role they had played in 1966 as direct suppliers of funds. Moreover, Federal agencies declined in importance as financial intermediaries during 1967.

In brief, the financial markets recovered from the turmoil of 1966 and continued the process of supplying an increased volume of funds to support the expansion of the economy. They did so at a historically high level of long-term rates, which indicated not only the strength of private demand for funds but also the expectation of continued expansion.

Supply: shifting channels

With the recovery of their lending ability, commercial banks and other financial institutions provided the principal channel for the $75-billion flow of funds raised in the financial system during 1967. Altogether these financial organizations provided $66 billion, as against only $41 billion in the preceding year of monetary restraint.

In early 1967, as monetary policy eased and lower rates developed in money-market and other short-term instruments, the competitiveness of these traditional financial institutions allowed them to attract funds diverted to other assets in the previous year. The public's bank deposits increased $33 billion, and an additional $17 billion went to deposits in other savings institutions. (Savings and loan associations recovered sharply, as their inflow of funds jumped from $4 billion to $12 billion.) With their increased resources, these institutions responded with increased lending — $35 billion for banks and $15 billion for other savings institutions. Insurance companies and pension plans supplied the remaining $17 billion in finance.

At the same time, the market showed less reliance on those sources which had helped bridge the financing gap of 1966. The U.S. Government supplied only $3 billion last year, down from nearly $8 billion in 1966, as the lending activity of its agencies slowed. Households, whose provision of a surprising $11 billion of direct finance was so critical in meeting the needs of 1966, turned around to unload securities acquired in that year. Household ownership of U.S. Government bonds, state-local bonds, and corporate stock fell, so that net security accumulation turned negative, down $5 billion. Instead of lending directly on the capital markets, households reverted to their more typical role of indirect lending, as they built up their deposits in commercial banks and other savings institutions by roughly $45 billion.

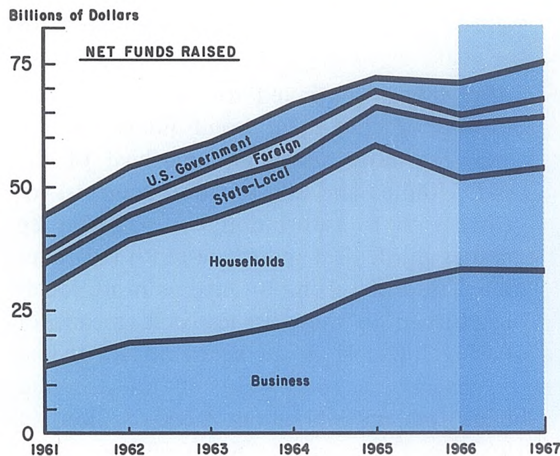
Private demand

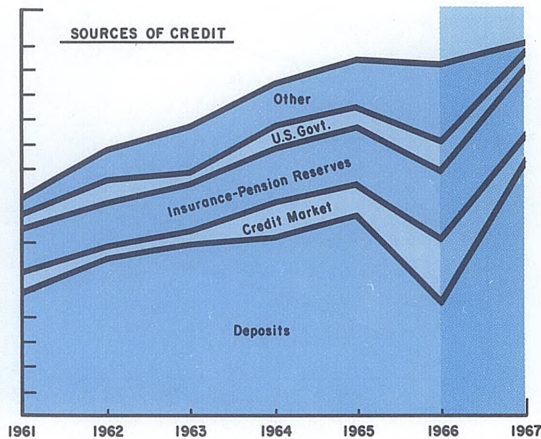
Private business demand (excluding that of financial institutions) was as usual the largest source of demand for finance in 1967. Private business borrowed $33 billion — 44 percent of total borrowing — thus matching the record high figure set the previous year.

Business capital expenditures fell off about $5 billion to about $90 billion in 1967. At the same time, gross business sav-

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Financial markets recover from '66 turmoil . . . private demand sluggish, while financial institutions regain usual dominant position on supply side





ing rose slightly to about $77 billion, thereby reducing somewhat the need for outside finance. Despite this increased flow of internal funds, a considerable borrowing requirement remained that was successfully financed, albeit at a record level of interest rates.

The mix of borrowing shifted during the year, as business placed greater reliance upon security financing while reducing its bank and mortgage borrowing. Corporate new issues reached a record $24 billion — 36 percent greater than 1966 and 60 percent above the 1965 figure. The vast bulk of this was debt financing, and as a result of this tremendous volume, interest rates on long-term corporate bonds rose steadily through the year. Altogether, manufacturing issues led with over $10 billion in new flotations, and public utilities followed with nearly $5 billion.

A clear-cut reduction occurred in household borrowing — a $3-billion decline to about $20 billion, the lowest level of borrowing since 1962. Total mortgage indebtedness rose by only $12 billion, compared with $14 billion in 1966 and a record $16 billion in 1964. Consumer credit grew at a slower pace — $5 billion as against $7 billion in the preceding year. In general, households slowed their accumulation of debt and increased their holdings of liquid financial assets, primarily bank deposits and other savings instruments, and thus ended the year in a more secure financial position.

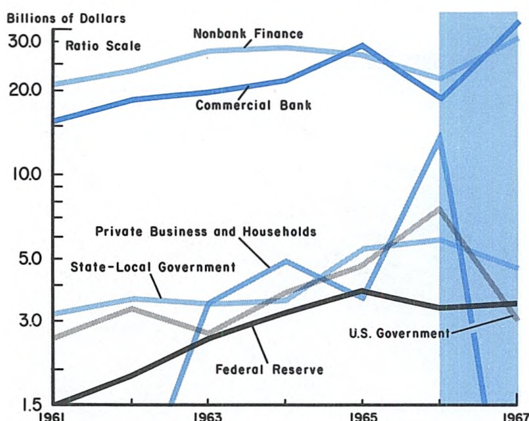
Government demand

The Federal government increased its net borrowing only marginally during 1967 to just above $7 billion, but some significant changes occurred in the composition of its borrowing. The various Federal agencies which had played such a vital intermediary role in 1966, particularly in supporting the mortgage market, recorded a large net reduction in new lending in 1967. The revival of lending power by private lenders reduced pressures on these agencies, and in turn permitted them to reduce their net borrowing by approximately $2 billion.

On the other hand, direct Federal borrowing increased by $5 billion as the Federal budget deficit expanded. But although Federal borrowing was very heavy in the second

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Market relies more on usual sources and less on those that bridged '66 gap



half of 1967, there was actually a more-than-seasonal retirement of Federal debt in the first half of the year. In contrast to 1966, when the Federal government acted as a giant financial intermediary, the bulk of Federal financing needs in 1967 arose from its spending operations rather than its lending activities.

State and local governments provided an even greater source of new demand for finance. These levels of government raised some $10 billion net, for a one-third increase over 1966, and thereby accounted for the largest increase on the demand side of the markets. This increase is typical of the decade-long trend of rising state and local borrowing. The trend was broken in 1966 when monetary restraint slowed borrowing, but with the 1967 easing, issues which had been postponed earlier reappeared in very heavy volume. The pace slowed somewhat in the latter part of the year, but in total, state-local bond sales jumped $3 billion for the year.

Education continued to be the principal purpose of state-local bond financing, absorbing a little less than one-third of the total. Utilities and conservation projects, together with transportation issues, made up another third. But industrial-aid bonds continued to grow in importance as more localities turned to these issues as a means of offering low-cost financing to attract industry. As late as 1965, sales of industrial-aid bonds totaled only about $200 million; in 1967, they were above $800 million.

In sum, 1967 was a year with a record volume of financing at record levels of interest rates. The mix of borrowing and lending was typical of an expansion year, 1967 resembling most other recent years in this regard. While there was a small decline in net private borrowing, the level attained was quite consistent with the upward trend established at the beginning of the decade. No doubt high interest rates restrained borrowing to some extent; nevertheless, financing records were set in such important sectors as the corporate-bond market even in the face of these high rates. The most buoyant element in the demand for funds was government borrowing—federal, state and local. In this and in several other respects, the 1967 pattern may well be repeated in 1968.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Banking '67 Style

Supported by a sharp rise in reserves, commercial-bank deposits and earning assets recorded their largest gains of the postwar period during 1967. The growth was accompanied, however, by a substantial shift in the composition of bank assets—a change which reflected the shift of business credit demands to the bond and commercial-paper markets, along with the increase in household mortgage borrowing from non-bank financial institutions such as savings and loan associations. As a consequence, and in contrast to their experience of the previous year, banks sharply expanded their holdings of Federal and state-local government securities. In fact, banks were virtually the only net supplier of funds to the public sectors.

Sharp deposit growth . . .

On the supply side of the ledger, the generally easier stance of monetary policy in 1967 was reflected in a sharp rise in member-bank reserves — a 10-percent increase between December and December. The gain was accompanied, too, by a sharp decline in borrowings from the discount window and by a turnaround in the banking system's reserve position, from net *borrowed* reserves of $271 million during the fourth quarter of 1966 to net *free* reserves of $177 million in the closing months of 1967.

However, the swing in the net reserve position had begun in late 1966, and by mid-1967 member-bank free reserves averaged about $300 million. Then, with the economy showing signs of accelerated growth, there was no further easing of reserve positions. Indeed, some evidences of tightening became noticeable in late 1967, including the raising of reserve requirements on member-bank demand deposits of over $5 million per bank (effective in January 1968).

Total deposits expanded in 1967 by about $34 billion, or almost 12 percent—well over double the 1966 increase. Furthermore, and in contrast to the previous year's $2-billion gain, demand deposits rose by $9 billion, and the total money supply (demand deposits plus currency held by the public) increased by $11 billion. But in 1967 as in 1966, time deposits accounted for the greater part of the increase in total bank liabilities, rising by $25 billion—double the previous year's gain.

Households accounted for most of the time-deposit increase, as they expanded their holdings of both passbook savings (in contrast to 1966) and higher-yield savings certificates. Towards year-end, however, the competitive pull of rising yields on alternative forms of investment was evident in a slower rate of growth in both types of accounts at banks.

For their part, businesses and other holders added about $4.7 billion to their holdings of large-denomination ($100,000 and over) certificates of deposit, following a net liquidation of about $0.6 billion during 1966. However, in this case too, some levelling off was evident towards year-end, as banks were unwilling or unable to match the rise in market yields generally. This rise carried yields on a wide range of instruments above the 5½-percent ceiling on certificates imposed by Federal Reserve Regulation Q, and thereby inspired fears of another round of disintermediation such as occurred late in 1966.

On balance, commercial banks in 1967 again garnered the lion's share of savings flows into depositary-type institutions — about 58 percent. This represented a reduction from the exceptionally large (two-thirds) share realized during 1966, but was still higher than the norm recorded during the earlier years of this business expansion.

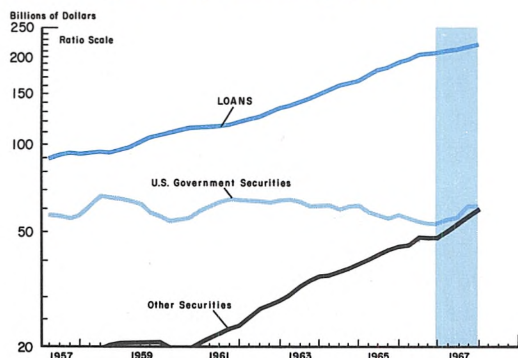
Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Slackened loan growth . . .

With their vastly expanded supplies of loanable funds, banks were able to increase their loans and investments at a fairly vigorous pace, with the result that outstanding commercial-bank credit rose in 1967 by about $35 billion, or 11 percent. Not only was this about double the rate of growth of GNP, but it was also about double the previous year's gain in bank credit. Furthermore, the banks' share of all funds supplied directly to the credit markets rose sharply to 47 percent in 1967 from only 27 percent in 1966 — the year of disintermediation. Moreover, the pattern of credit allocation differed markedly from that of 1966.

Business loans, which had risen by 13 percent in 1966 on the heels of an even larger increase in 1965, rose at a more sedate (9-percent) pace in 1967. Five of 22 major classified industry sectors made net repayments of loans to large banks during the year. (These industries included textiles, apparel and leather, transportation equipment, construction, retail trade, and foreign business firms.) Nine other industry groupings increased their borrowings by less than in 1966 — and in most cases by substantially less. In fact, aside from a sharp rise in bankers-acceptance financing, the only sectors which improved on their previous year's performance were commodity dealers, petrolelum refiners, and primary-metals manufacturers.

Banks show moderate rise in loans but bulge in investment portfolios



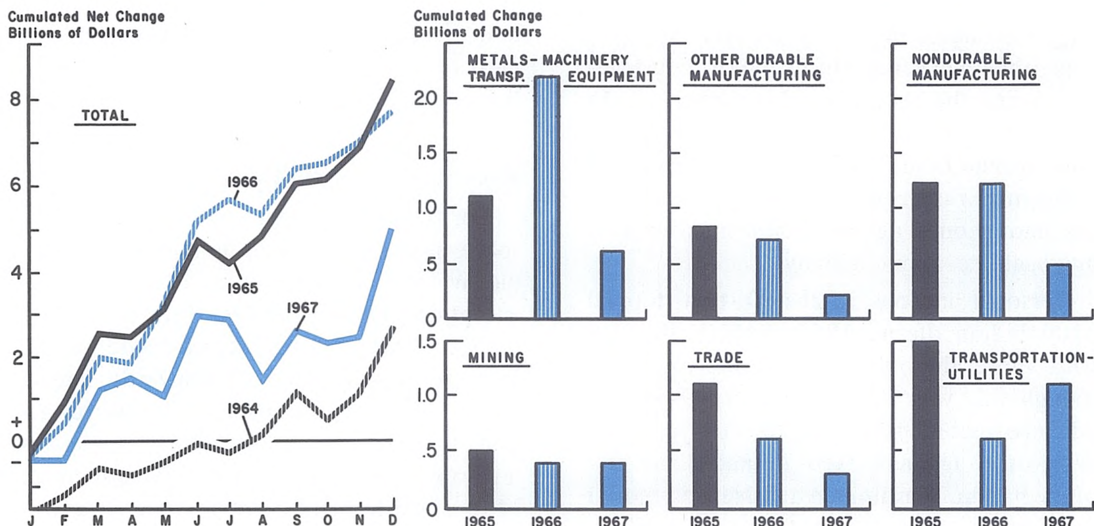
This slowdown in business borrowing reflected a shift of corporate financing to the commercial-paper market, and even more particularly to the bond market, as corporate treasurers sought to stockpile long-term funds in anticipation of further increases in borrowing costs and taxes. However, the slowdown also reflected the sharply reduced pace of business inventory accumulation in 1967. In any event, banks financed only one-sixth of business' external credit requirements in 1967, compared with one-third in 1966 and two-thirds in 1965.

At the same time, the cost of business borrowing trended downward in 1967, following a succession of increases in the prime rate to 6 percent in August of the previous year. By April, the prime rate had generally eased to 5½ percent, where it remained until after the November increase in the discount rate. Meanwhile, the weighted average rate on short-term business loans, as reported by banks in 35 centers throughout the nation, declined to 5.96 percent in November from 6.13 percent in February.

Consumers, like businesses, also reduced the pace of their bank borrowings in 1967 as consumer loans rose by only $2.5 billion — much less than the average increment of the preceding five years. Furthermore, and in contrast to 1966, the increase centered in credit-card and similar financing rather than automobile financing. But in spite of the reduced growth, banks still increased their share of the total consumer-credit market, from 45 to 52 percent. On the other hand, a $4-billion increase in banks' mortgage financing still meant a reduction in the banks' share (from 24 to 19 percent) of the overall mortgage market. This reduction largely reflected the sharp expansion in home mort-

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Businesses exhibit much smaller reliance on bank loans during 1967 than during 1965-66 durable-goods manufacturing boom



gage financing by savings and loan associations, as S&L's recovered from the exceptionally depressed levels reached the previous year.

. . . and bulging investment portfolios

While loans to businesses and consumers thus moderated from the vigorous pace of the two preceding years, commercial banks sharply expanded their holdings of debt instruments of Federal and state-local governments in 1967. Banks added more than $6 billion to their holdings of U.S. governments —a 12-percent increase—after three successive years of liquidating governments in order to finance the burgeoning credit demands of business and other private sectors. Meanwhile, bank holdings of tax-exempt issues rose even more sharply — by about $11 billion or 25 percent. Thus, commercial banks in 1967 absorbed virtually the entire net increase in both types of government debt, and thereby accounted for the sharp rise in the banks' share of total credit-market financing.

Commercial-bank liquidity improved during the year, since loans rose less rapidly than deposits, and since a substantial portion of banks' newly acquired securities consisted of short-term government obligations. The ratio of loans to deposits declined from a post-war high of about 66 percent at year-end 1966 to 64 percent at the end of 1967. (The ratio dropped from 84 to 80 percent at New York Reserve City banks.) The ratio of short-term U.S. governments to deposits at all commercial banks also improved, rising from 6.1 percent to 6.5 percent over the same time span.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Outpacing the Nation

The Western economy was something of a paradox in 1967, showing signs of sluggishness in several of its major industries, yet ending the year with pluses over-all. In terms of personal income, retail sales, and employment, the Twelfth District economy performed rather well; in fact, it outpaced the nation once again in these measures of aggregate economic activity.

Personal income in the District topped $100 billion during 1967, ending the year with more than a 7-percent increase. Although this was below the sharp 9-percent advance recorded in the previous year, the West once again in 1967 outpaced the rest of the nation. Washington and Nevada scored the largest gains, while California—which normally accounts for roughly two-thirds of District income—about matched the average U.S. increase.

The income differential between the District and the nation was reflected in the retail-sales statistics. Whereas sales in the nine Western states increased 5 percent during 1967, the national gain was only 3 percent. The regional strength in retail sales was centered in autos and other durable-goods stores.

Backing up these gains in income and consumption was a 3-percent increase in District employment. Nearly all sectors showed increases for the year, even though the over-all gain was the smallest since 1964 and considerably below the 5-percent expansion of 1966. The brightest spot was construction, which recorded an employment rise for the first time in four years.

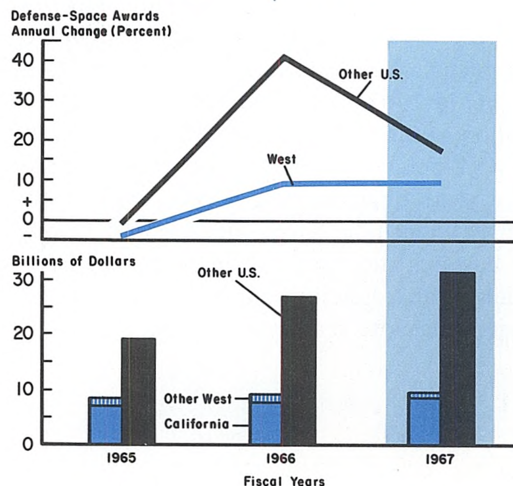
On the other hand, both agriculture and mining lost employment during the year; the latter industry, of course, was hit hard by the prolonged copper strike, and farm employment has been on a downtrend for several years. And with the usual additions to the labor force, the District's unemployment rate (4.6 percent) remained stubbornly close to the jobless figure for 1966.

Aerospace — still flying high

For the past few years, the District's aerospace industry has been a stalwart leader in the Western economy — and 1967 was no exception. During the first three quarters of the year, District firms recorded a 15-percent increase in defense contract awards, and almost one-half of the increase in awards nationally went to District firms — as against only a one-tenth share of the 1966 increase. Most of the District's growth in defense work was centered in California, while Washington registered a slight decline.

Although the regional industry received fewer awards from the national space agency, employment was bolstered by the boom in commercial jet-aircraft. The commercial sector was beset by production and

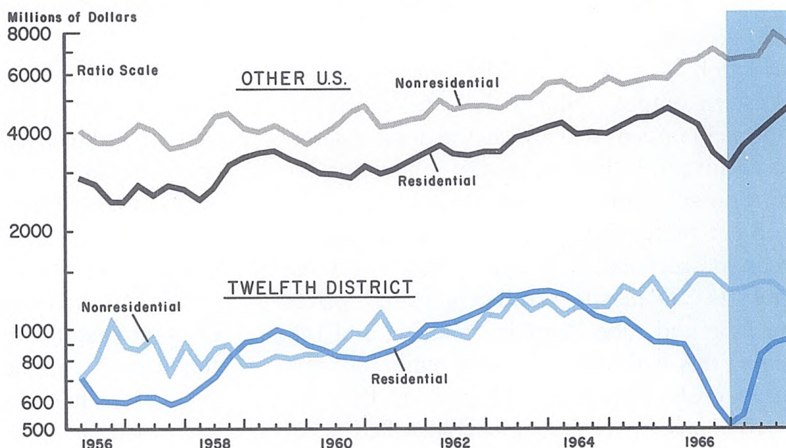
Defense sector dominates business activity, in West as elsewhere



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

scheduling problems in the early part of the year, but it recovered in subsequent months to show a modest employment gain for the year. Order backlogs remained large for both subsonic aircraft and the new supersonic transport. So far, 107 delivery positions have been reserved for the American SST — and in view of the speculation that the French-British Concorde is experiencing financial difficulties, the market for the U.S. supersonic entrant may be further broadened.

Western housing industry recovers from slump, but nonresidential activity drops below earlier peak



Up from the depths — slightly

Nothing comes easy for the District's construction industry. In 1966, non-residential and heavy engineering construction expanded while residential construction plummeted, but in 1967, their positions were almost reversed. As a result, *total* construction activity grew only slightly during the year, and thereby fell behind the national pace.

Nevertheless, housing starts in the West posted an almost uninterrupted succession of gains throughout August, before showing signs of leveling off. For the year as a whole, housing starts totaled 221,000 units, a 14-percent gain over 1966 and considerably better than the 9-percent average increase recorded elsewhere.

A noteworthy development was the recovery of multiple units. Building permits for these dwellings topped the 1966 volume by about 30 percent, compared with a gain of 11 percent for single-family structures.

Non-residential and heavy construction, on the other hand, failed to maintain the strong pace of the several preceding years. Only Arizona, Utah, and Washington showed non-residential gains, while all other District states lagged in this category.

Lumber and steel

Despite decided improvement in housing activity, the Western lumber industry underwent its second year of declining output and employment. After responding briefly to the housing upsurge early in the year, lumber output began to decline in the spring in the face of a slowdown in demand (and other factors) and it dropped even further when August's disastrous forest fires created a shrinking log supply.

But by mid-summer, the improved housing market and the decline in lumber output led to strong upward pressures on Douglas-fir prices. These pressures intensified in the late fall as unseasonably mild weather in the East and Midwest permitted construction in those areas to continue at a good pace.

District construction activity also had an impact on the Western steel industry, which finished the year with an output of 6.6 million tons — about 3 percent below 1966's record high. Although regional producers

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

escaped most of the effects of the automobile and steel-hauler strikes, the decline in demand for structural steel — associated with the slowdown in industrial and heavy construction — made a decided impression on Western output. Nonetheless, total production rebounded sharply in the final quarter as an inventory buildup began in anticipation of a possible mid-'68 steel strike.

Steel prices continued to rise during the year, despite the persistent threat of foreign imports. Domestic producers raised prices on pipe and tube items in January, and followed this with hikes on steel plate and bars in August. Finally, in December, they increased prices for hot and cold-rolled sheet and strip by $5 a ton. Consequently, the finished-steel price index rose about 2 percent during the year.

Farmers and canners — contrasts

The District's crucial agricultural industry about matched its previous year's performance with $6.5 billion in marketing receipts. California and Arizona crop production was severely affected by the damp spring, which reduced the output of deciduous fruits and early spring vegetables. Cotton production also suffered from the unfavorable weather, as well as from insect damage. In contrast, the abundant moisture benefitted District grain farmers; high yields, combined with a sharp increase in acreage, boosted wheat production in the Pacific Northwest by about one-third.

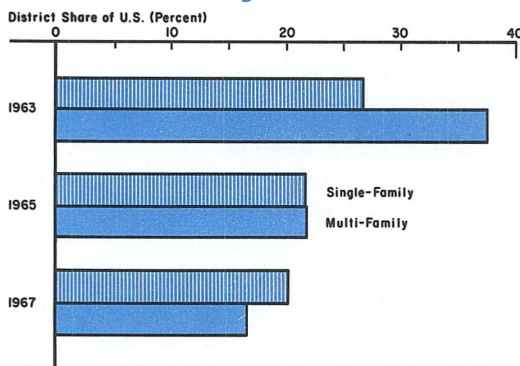
Livestock marketings fell considerably below the year-earlier level, primarily as a result of reduced sales from California feedlots. Poultry and egg production increased substantially, however, and hatchings of both broiler chicks and turkey poults were more plentiful than a year earlier.

Western canning activity also was a study of contrasts. Total production dropped from the record volume of 1966 because of the poor fruit harvest, but the vegetable pack surpassed the previous high of 102 million cases processed in 1956. Tomato production continued to grow, and 80 percent of the crop was harvested by machine.

Dampened by spring rains, the fruit pack was the smallest since 1958. In California, the output of cling peaches dropped from 30 to 23 million cases, and canned-pear output plummeted from 6 million to 1 million cases over the year.

With the reduction in supplies, canners paid substantially higher prices for their raw materials. Pears, for example, jumped from $95 a ton in 1966 to $150 in 1967. Tomato prices also climbed, from about $36 to $45 per ton, despite rising production.

Despite recovery, Western share of national housing market declines



Metals and oil — mixed

The District's nonferrous-metals industry was severely hampered by the prolonged copper strike, which idled 25,000 mine and smelter workers and brought copper production to a standstill throughout the second half of the year. Copper production dropped more than one-third below the 1966 figure, and the drop would have been even greater except for a significant increase in output during the early months of 1967.

Copper shortages did not begin to appear

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

INDEXES OF INDUSTRIAL PRODUCTION — TWELFTH DISTRICT

(1957-59=100)

INDUSTRIAL PRODUCTION	1960	1961	1962	1963	1964	1965	1966	1967
Copper	112	119	127	128	129	140	146	90
Lead	76	99	105	103	96	93	118	96
Zinc	86	97	101	98	93	89	96	87
Silver	91	105	105	105	102	114	131	100
Gold	99	92	86	86	85	116	135	103
Steel Ingots	102	111	100	117	132	138	140	136
Aluminum	101	97	107	118	135	150	165	195
Crude Petroleum	95	96	96	97	97	102	112	121
Refined Petroleum	104	108	111	112	115	120	122	126
Natural Gas	112	121	127	144	148	147	158	172
Lumber	98	95	98	98	108	107	103	97
Douglas Fir Plywood	120	132	142	160	177	180	180	—
Canned Fruit	111	116	121	108	141	109	135	105
Canned Vegetables	101	89	106	96	100	97	113	115
Meat	107	111	112	115	126	126	130	131
Sugar	105	107	113	120	138	137	132	116
Flour	102	99	101	94	96	92	91	91
Creamery Butter	112	120	119	103	103	96	85	105

until late October, however, principally because of large stocks on hand and increased imports. But at that point, the dealer price of refined copper shot upward to 64 cents a pound, almost 20 cents above its pre-strike level.

The strike also affected the market for silver, which is generally produced as a by-product in copper and other metal mining. Domestic and international shortages, along with the lifting of the U.S. Treasury's $1.293 ceiling in mid-year, were reflected in a steady climb of prices, climaxed by a record $2.17-an-ounce quotation on the New York market in late November.

The aluminum industry fared somewhat better during the year, as new productive capacity in the Pacific Northwest enabled producers to achieve a record output of the metal. The threat of overproduction appeared in the second and third quarters as shipments dropped off, but demand recovered somewhat in the final quarter.

Petroleum refining activity came under pressure in mid-1967 as a result of the embargo on petroleum shipments by Arab countries. Normally the District depends upon imports, primarily from the Middle East, for almost one-third of its crude oil supplies. Thus, in order to maintain refining activity during the affected period, Western refineries obtained increased supplies from sources within the District and from Canada. Over the year, crude oil production in the District increased nearly 7 percent, or 25 million barrels, with most of the gain coming from California, Alaska, and a new field in Arizona.

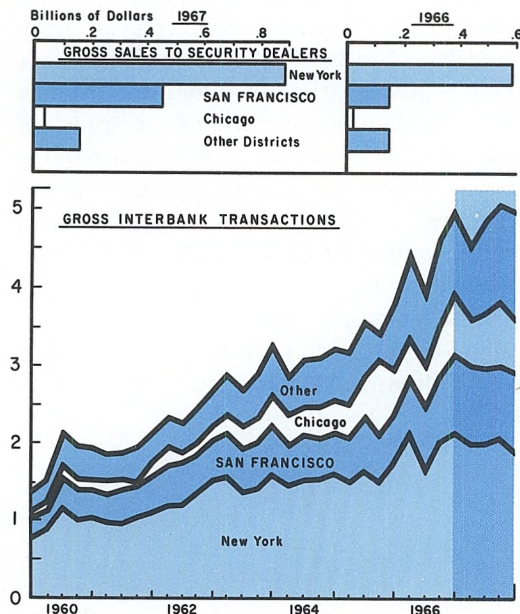
Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Calmer Sailing

Western banks had relatively calm sailing in 1967 after the turbulence of the preceding year, and they managed to record a sharp gain in outstanding bank credit during the year. Large District banks expanded their loan portfolios by 5 percent —just one percent short of the 1966 gain —and they increased their holdings of securities by 18 percent. Therefore, total bank credit expanded over 8 percent — nearly double the rate of increase in the preceding year.

The severe competition for time-and-savings deposits which had characterized earlier years modified somewhat in 1967, as savings-and-loan associations as well as banks now operated under legal interest-rate ceilings on deposits. In a reversal of the 1966 experience, large District banks gained passbook savings as well as consumer-type certificates, and overall reported an 11-percent increase in total time-and-savings deposits. District banks lagged behind the national pace in this category; on the other hand, they matched the performance of large banks elsewhere with a 6-percent increase in demand deposits adjusted.

Fed-funds activity centered in New York and Western banks



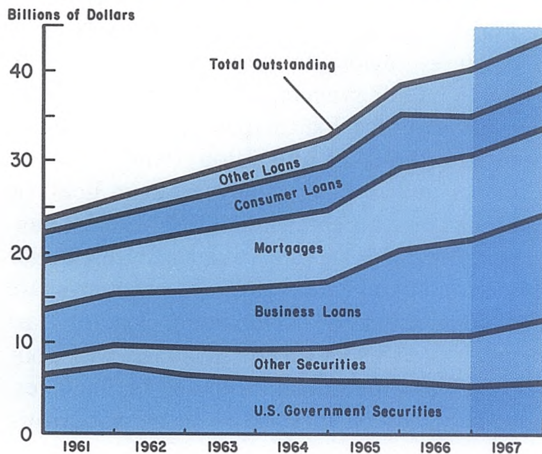
During 1967, Western banks were fairly successful in repairing their liquidity positions, which had been depleted during 1966. In the first half of the year, large District banks made heavy acquisitions of municipals, and about one-fourth of these holdings at midyear carried maturities of one year or less. In the latter half of the year, banks also added to their short-term holdings of U.S. Government issues. Thus, these increases in short-term securities bolstered their ability to meet future loan demands. Also, the less rapid loan expansion and increased deposit inflow last year reduced the loan-deposit ratio of large District banks from 72.3 to 69.6 percent between December 1966 and December 1967.

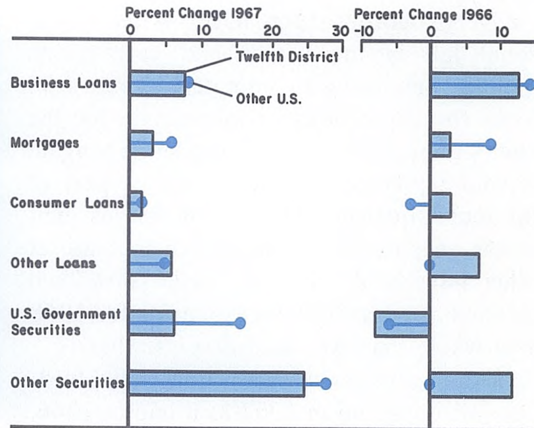
According to still incomplete data, 1967 was a year of record earnings for many banks in the West. Interest-rate ceilings on time-and-savings deposits helped curb the rapid spiral in bank costs, and this was especially important in the District, since Western banks traditionally hold a high proportion of time-and-savings to total deposits. In addition, revenues of District banks increased along with those of other banks when the prime rate of 5½ percent was pushed back up to 6 percent late in the year, at a time when business-loan demand was also strengthening. Heavy investment in relatively high-yield municipal securities also helped to increase the after-tax revenues of Western banks.

Only six new banks were established in District states in 1967, and this growth was more than offset by 23 mergers and consoli-

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

District bank credit expands twice as fast in '67 as in '66, on strength of small gain in loans and sharp rise in security holdings





dations. Thus, 1967 witnessed a further net reduction of 17 in the number of banks operating in the Western states. On the other hand, 208 new branches were established and 9 were closed during the year, as against 170 branch openings and 5 closings during 1966.

Some reserve pressure

The reserve position of District member banks was slightly easier in 1967 than in the tight-money year, 1966, but the swing was not as pronounced for Western banks as it was for other member banks. In fact, during the first and again during the fourth quarter, District bank borrowings from the Federal Reserve Bank were greater than their reserves in excess of requirements. For the year as a whole, excess reserves of District banks averaged $26 million while borrowings from the discount window averaged $21 million — ranging from a high of $33 million in the first quarter to a low of $8 million in the third quarter. Thus, banks recorded average *free* reserves of $5 million for 1967 as compared with net *borrowed* reserves of $4 million in 1966. (All data are on a daily average basis.)

Continuing reserve pressure on District banks also was evident in the relatively high volume of borrowing from other banks through purchases of Federal funds (idle balances of banks on deposit with Federal Reserve Banks) and from corporations under repurchase agreements. In 1967, large District banks averaged $416 million in net interbank Fed-funds purchases (as against only $9 million in 1966), but a large proportion of these purchased funds were resold to U.S. Government securities dealers.

West Coast banks accounted for one-fifth of the total volume of gross interbank transactions by large banks in 1967. This area thus continued to rank second — next to New York City — as a money-market center for Fed-funds transactions. Furthermore, these Western banks accounted for almost one-third of Fed-funds sales to U.S. Government securities dealers—a substantially broader participation in this sector of the money market than heretofore.

Strong business demand

Business loans, with a $778-million (7-

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

percent) increase, were the dominant factor in the 1967 loan growth of Western banks, although business demand lagged behind the very vigorous 1966 pace. After a seasonal lull in the winter and early-spring months, borrowing by commercial-industrial firms rose by a near-record volume for the June tax period, and then rose sharply again in mid-September and in the latter part of the fourth quarter. The gain in the last half of the year exceeded the rate of increase at other large banks, but the earlier slowdown resulted in a smaller loan expansion for 1968 as a whole than was recorded elsewhere.

The durable-goods sector dominated business-loan demand in 1967 as it had in 1966. Machinery manufacturers increased their bank debt more than other durable-goods processors, but transportation-equipment manufacturers — the large borrowers in 1966 — made net repayments. Loans to public utilities accounted for another large portion of the loan expansion. Meanwhile, in a reversal of the 1966 trend, Western banks added substantially to their holdings of bankers acceptances during 1967. Incidentally, banking offices outside the major metropolitan centers garnered a larger share of the expanded commercial lending last year, whereas the 1966 increase was concentrated predominantly in the major cities.

The cost of short-term business borrow-

SELECTED ASSET AND LIABILITY ITEMS OF WEEKLY REPORTING LARGE BANKS IN THE TWELFTH FEDERAL RESERVE DISTRICT

(dollar amount in millions)

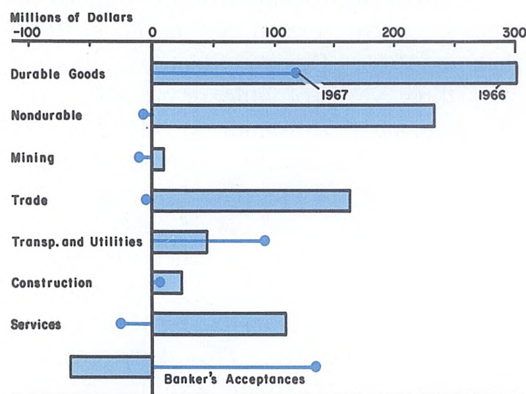
	Twelfth District Outstanding Dec. 27, 1967[1]	Twelfth District Net Change Dec. 28, 1966 to Dec. 27, 1967		Twelfth District Net Change Dec. 29, 1965 to Dec. 28, 1966	Other U. S. Net Change Dec. 28, 1966 to Dec. 27, 1967
		Dollars	Percent	Percent	Percent
Total loans and adjustments	$44,420	+3,540	+ 8.7	+ 4.5	+ 10.7
Loans adjusted and investments	43,599	+3,338	+ 8.3	+ 4.5	+ 10.4
Loans adjusted	30,754	+1,430	+ 4.9	+ 5.8	+ 6.5
Commercial and industrial loans	11,556	+ 817	+ 7.6	+ 12.3	+ 8.5
Real estate loans	9,544	+ 303	+ 3.3	+ 2.3	+ 6.2
Agricultural loans	1,207	+ 65	+ 5.7	+ 1.7	+ 6.3
Loans to nonbank financial institutions	1,631	+ 16	+ 1.0	— 9.8	— 3.9
Loans for purchasing or carrying securities					
To brokers and dealers:	445	— 64	— 12.6	—121.3	+ 16.1
To others:	196	+ 27	+ 16.0	— 0.6	+ 16.7
Loans to foreign banks	260	— 37	— 12.5	+ 0.3	— 8.4
Consumer instalment loans	4,486	+ 124	+ 2.8	+ 3.7[2]	+ 2.0
All other loans	1,826	+ 218	+ 13.6	0	+ 8.9
Total investments	12,845	+1,908	+ 17.5	+ 1.2	+ 20.5
U. S. Government securities	5,567	+ 317	+ 6.0	— 8.0	+ 16.0
Treasury bills	1,056	— 1	— 0.1	+ 2.9	+ 33.9
Treasury certificates of indebtedness	0	— 99	—100.0		—100.0
Treasury notes and bonds maturing:					
Within 1 year	733	+ 96	+ 15.1	— 17.8	+ 19.5
1 to 5 years	2,636	+ 617	+ 30.6	+ 2.6	+ 35.0
After 5 years	1,142	— 296	— 20.6	— 25.8	— 28.7
Other Securities	7,278	+1,591	+ 28.0	+ 11.5	+ 24.8
Total deposits (less cash items)	43,833	+3,689	+ 9.2	+ 3.6	+ 11.2
Total demand deposits (less cash items)	16,494	+ 999	+ 6.4	— 1.7	+ 7.0
Demand deposits adjusted	15,004	+ 788	+ 5.5	— 2.3	+ 5.8
Time and savings deposits	27,339	+2,690	+ 10.9	+ 7.1	+ 16.1
Savings deposits	15,615	+ 496	+ 3.3	— 8.5	+ 2.9
Other time deposits IPC	7,736	+1,672	+ 27.6	+ 92.0	+ 33.4
Capital accounts	3,568	+ 130	+ 3.8	+ 2.0	+ 6.7
Total assets/liabilities and capital accounts	54,764	+4,731	+ 9.5	+ 6.1	+ 11.4

[1] Revised data

[2] Partially estimated

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Durable-goods sector continues to dominate business-loan demand



ing declined in Western metropolitan areas during most of 1967, from an average rate of 6.28 percent in the first half of February to 5.97 percent in the first part of November. However, the November increase in the prime rate, to 6.00 percent, immediately led to higher business borrowing costs and to increased pressure on other loan rates as well.

Mortgage upturn

Western banks and savings-and-loan associations posted sharp gains in mortgage lending in 1967, with the help of increases of 10 percent or better in their savings inflows. Despite a first-quarter decline, commercial banks improved slightly on their 1966 performance with a $303-million increase in mortgage loans, while S&L's expanded their mortgage portfolios by about $1.4 billion — three times the gain recorded in 1966. Banks undoubtedly would have scored a larger gain if they had not stepped up sales of mortgages from their own portfolios to insurance companies and other institutional investors.

These developments were accompanied by a firming in mortgage yields following some early-year sluggishness. In the West, yields on 6-percent 30-year FHA mortgages recovered an earlier 50-basis-point decline and rose to 6.77 percent in December, while yields on conventional mortgages for new homes rose to 7.00 percent. In both cases, rates were only slightly below those reached at the interest-rate peaks of 1966.

Furthermore, the net growth in savings at District S&L's gave signs of tapering off in the last half of 1967, partly because of the competitive pull of rising yields on market instruments and the mid-year rollback on interest rates payable by associations in several major Western states. By year-end the spread between the bellwether 90-day Treasury bill rate and the rate on S&L passbook accounts, which had favored the latter by as much as 190 basis points in June, was reduced to about 13 basis points, thereby prompting concern over the possibility of another round of disintermediation such as occurred in 1966. The growing signs of money-market weakness also contributed to a slower increase in new mortgage-loan commitments on the part of liquidity conscious S&L's; the December volume of commitments was only slightly higher than the June figure, following a sharp increase in the first half of the year.

Consumer caution

Despite the proliferation of credit-card plans, overdraft privileges, and other special plans designed to encourage consumer borrowing, Western consumers continued in a cautious mood throughout 1967. Consumer instalment credit at large Western banks rose by $124 million—a 3-percent gain, as against the previous year's almost 4-percent increase — thereby reflecting the many uncertainties (political, civil, and economic) which plagued Westerners as well as other Americans during the year. As a consequence, the many special procedures instituted by Western banks to facilitate borrowing in the highly competitive consumer

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

area did not show spectacular results last year, although they may well do so after this initial breaking-in period.

District bank lending in other sectors followed divergent patterns last year. The level of loans to non-bank financial institutions remained consistently below the level of 1966 (except for December) as sales- and personal-finance companies increased their reliance on the commercial-paper market to meet their borrowing needs. On the other hand, loans to brokers and dealers for financing U.S. Government securities generally ran substantially above the year-before pace throughout 1967. Agricultural loans, with a 6-percent year-to-year gain, also remained substantially above the 1966 level.

Popular municipals

Large banks took advantage of the early-1967 breathing spell to expand their security holdings again after the erosion of the preceding year. However, U.S. Government securities accounted for only one-sixth of the $1.9-billion expansion in investments. District banks ended the year with only a nominal change in their Treasury-bill holdings, but they recorded a substantial shift from long-term bonds into issues maturing in one-to-five years, along with some increase in securities with maturities of one year or less.

Municipal obligations, with their very attractive after-tax yields, accounted for the bulk ($1.2-billion) of the increase in bank security holdings. Purchases were concentrated in tax warrants and other short-term issues, along with substantial amounts of state-local bonds with maturities of one year or less. Thus, the improvement in banks' liquidity positions centered largely in the municipal segment of their portfolios. During the year, Western banks also favored Federal Agency participation certificates, increasing their PC holdings by $167 million.

Rapid deposit growth

Total deposits of large Western banks increased almost three times faster in 1967 than in 1966. Demand deposits adjusted, after three years of little or no gain, rose 5½ percent ($788 million) in 1967. In addition, time-and-savings deposits expanded by $2,690 million. The 11-percent gain in this category was considerably greater than the increase in 1966, when disintermediation held the expansion to 7 percent despite higher rate ceilings on certificates during most of that year. This sharp increase in savings inflows, along with the parallel increase in S&L inflows, made possible the strong recovery in District mortgage activity over the year.

A major development in bank time-deposit behavior was the reversal of the decline in passbook savings, beginning in the spring of 1967 and continuing throughout the year. As passbook savings rose, however, the rate of expansion in consumer-type time deposits declined. Moreover, a net reduction occurred in the fourth quarter as Christmas Club accounts were paid out and as substantial withdrawals were made to meet property taxes and prepaid California income taxes.

In the first quarter of 1967, Western banks posted a $655-million net gain in large-denomination negotiable CD's, but deposits of this type declined during most of the rest of the year as their rates began to push against the legal ceiling of 5½ percent. Still, for 1967 as a whole, the banks had a $528-million year-to-year increase.

In the public-funds category, District banks fared better in 1967 than in the preceding year, as time deposits of states and political subdivisions rose $213 million over the course of the year. In fact, prior to the usual seasonal runoff in April, public deposits topped $3 billion for the first time in history.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Catalog of Expansion

The diverse regional economies which make up the nine-state District continued to expand during 1967. The pace was not quite so rapid as it was in over-exuberant 1966, but ample evidence of the broad-based strength of the boom can be garnered from the long catalog of expansionary items listed below.

Diversity as well as strength showed up in regional employment data. The Pacific Northwest and Southern California both increased by roughly 4-percent during the year, and other District areas scored increases of 3-percent or more — roughly in line with the performance of the rest of the national economy.

Bank loan data exhibited a slower-than-national pace, just as in the several preceding years. The slowdown centered in California member banks, where net loans increased 3½-percent, or somewhat more slowly than they did in either 1965 or 1966, partly because of the early '67 sluggishness in mortgage lending. Pacific Northwest and Mountain states meanwhile stepped up their lending pace, with better than 7½-percent gains.

Retail prices in major Western cities reflected both the early-year sluggishness and the late-year upsurge in business activity. The accelerated climb began in the spring months, as food prices reversed a six-month decline, and continued through the year, augmented during the summer by increases in California cigarette, liquor, and retail sales taxes. (Other contributing factors were higher price tags on apparel and automobiles, rising homeowner costs, and the continued uptrend in consumer services.) For the year as a whole, the Seattle and San Francisco indexes slightly exceeded the national increase of 2.8-percent. Los Angeles consumer prices rose by 2.5-percent — but here as elsewhere, the increase was the greatest since the beginning of the decade.

CALIFORNIA

Aerospace Both military and commercial orders helped to sustain aerospace activity in California last year. Defense procurement awards amounted to $6.7 billion in the January-September period alone. The list included the following: $65 million for P3B aircraft; $51 million for Polaris A3 missiles and $35 million for engineering services on the fleet ballistic-missile system; $25 million for the Poseidon intercontinental ballistic missile; $32 million for the Redeye shoulder-fired battlefield missile; $675 million for the Manned Orbiting Laboratory Program; $170 million for the Apollo Lunar Launching Program; $64 million for the nuclear rocket-engine program; and $29 million for 8 C9A hospital planes.

Commercially, the jumbo jet is the main concern of many California-based aerospace companies. And although the prime contract for the supersonic transport went elsewhere, a large proportion of sub-contracts, estimated at $1.4 billion over the 5-8 year development period, have been placed with California firms.

Steel During 1967, the state's only fully integrated producer announced its intention to increase its steel-making and fabricating capability by one-fifth, at Fontana. Plans call for the construction of a new plant for the manufacture of raw steel, modernization of existing bar and continuous-weld pipe facilities, construction of a cold-rolled sheet mill and a facility for the manufacture of tinless tinplate.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Another major producer plans to build a structural steel fabricating plant on a 129-acre site adjacent to its Pittsburg works. And a third major company will make its initial entry into the Western market with a plant — reportedly Northern California's first fully integrated facility — on a 3,300-acre river-front site in Solano County, about 40 miles northeast of San Francisco.

Petroleum and gas A number of significant developments were recorded by California's petroleum and gas industry in 1967. Total crude capacity reached over 1 million barrels a day, and expansion was continued. Scheduled for completion in 1969 are a 70,000 b/d refinery at Benicia and a $100-million unit at El Segundo.

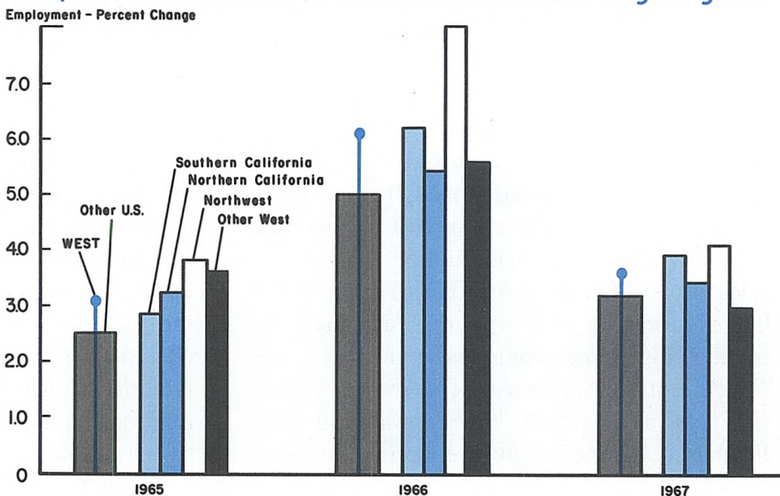
Construction Large residential-commercial projects recovered along with the rest of the construction industry in 1967. Among the projects planned or underway were: the $300-million Marincello community in Marin County; the $220-million Serramonte Planned Community in Daly City; the $150-million Embarcadero Center in San Francisco; the $120-million Atlantic-Richfield Plaza complex in Los Angeles; and the $100-million Silverado project in Napa Valley.

Hospital facilities and educational edifices continued to rise in nearly every community. At Stanford University, 1967 saw the completion of a $114 - million Linear Acceleration Center. Plans were laid for the construction of a $38-million auditorium - exhibition center in downtown Los Angeles, and extensive hospital construction is in progress in Torrance, Santa Ana, Santa Rosa, Fresno, San Jose and Oakland.

Shipping Worldwide attention was focussed on Long Beach when that city purchased the *Queen Mary* for $3.5 million. At a further cost of $1.5 million, the famous ship will be converted into a 400-room hotel and a "Museum of the Sea." Following this up, San Francisco and other cities are now planning to bid on the *Queen Elizabeth.*

The expanded use of efficient containers for freight shipping was a boon last year both to ship-builders and to port construction. One large shipping concern has begun a $100-million replacement and conversion program which will increase its container-ship capacity by 50 percent within the next few years. Another firm is planning to build a $45-million fleet of three 24-knot container-ships for service in the Pacific; each ship will have a cargo capacity of one million cubic feet.

The ports of Long Beach and Los Angeles have long-term plans to increase vessel capacity by 150 percent. San Francisco has completed its $23-million Army Street



Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Terminal. In Oakland, the $30-million 7th Street Terminal will add 10 deepwater berths when completed in 1969, and 8-12 more berths will be added later on.

Public utilities The California Department of Water Resources, in conjunction with the city of Los Angeles, has substantially expanded plans for hydroelectric pump and storage facilities to be built in Los Angeles County. The revised plan would increase investment in the California Aqueduct Project to $1.7 billion from the earlier estimate of $1.2 billion. It would generate 1.6 million kilowatts of electric power — instead of 523,000 kilowatts as originally intended — and would provide for the construction of four dams and reservoirs.

A major utility firm has announced plans to build a nuclear power plant near Diablo Canyon in San Luis Obispo County. The cost would be $150 million and capacity would exceed one million kilowatts. This firm, incidentally, expects to double the size of its overall $4.2-billion plant within the next 10 years. In Southern California, another major utility expects capital spending to exceed $640 million over 1967-68. As part of a 5-year expansion program, the company is now constructing several steam-generating plants that, when finished, will add about 900 megawatts a year to its operating capacity.

In the planning stage are several major projects: a $200-million, one-million-kilowatt nuclear generating plant in Santa Barbara County; and a $169-million generating station consisting of two 750,000-kw units near Oxnard.

Transportation Bridge and highway construction reached a record level last year in California. Major projects included: $27 million for a 4-lane high-level bridge to replace Dumbarton Bridge between Alameda and San Mateo Counties; $14 million for a 6-mile section of the Interstate freeway between Stockton Channel and Hammer Lane in San Joaquin County; and $14 million for an overpass, ramps and roadways in Long Beach.

Plans are already being formulated by California's major airports to service the expected flood of traffic that will accompany the introduction of jumbo and supersonic transports. Los Angeles plans to spend $500 million over the next eight years for a regional airport system, San Francisco has a $98-million master plan, and at Oakland, an $11-million maintenance hangar, the largest in the nation, will be built in 1968.

Construction of the Bay Area Rapid Transit system — scheduled for completion in 1972—progressed somewhat slowly during 1967. Major work was done on aerial structures in Oakland, a 4-mile tube at the bottom of the Bay, and a tunnel through the East Bay hills.

In Los Angeles, the Southern California Rapid Transit District (SCRTD) has proposed the spending of $1.6 billion for a 62-mile rapid transit system and augmented bus service facilities (completion date 1975). This huge project, involving the purchase of 475 rapid-transit cars and 300 new buses, would carry up to 327 million passengers annually by 1980.

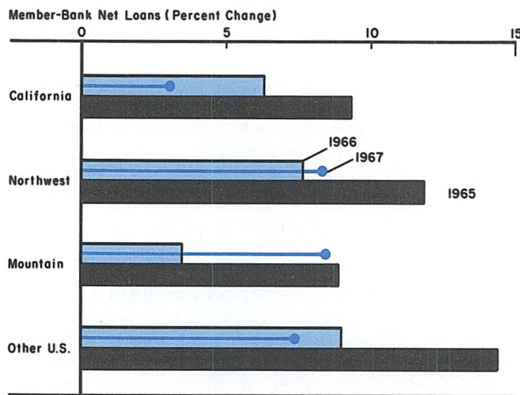
PACIFIC NORTHWEST

Aluminum Undaunted by a slight setback in industry-wide shipments in 1967, aluminum producers stepped up their plan to expand primary and fabricating capacity. Altogether, Pacific Northwest aluminum capacity is expected to reach 1.5 million tons a year by 1972, up from 600,000 tons in 1955 and one million tons in 1967.

A new entrant into the field began work on a $142-million project at Warrenton,

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Bank lending pace slows in California but not in other Western areas



Oregon; this project eventually will include a 130,000-ton reduction plant and an alumina plant to process bauxite brought in by ship from Australia. Another new producer, after completing a reduction plant at Bellingham, Washington, readied plans to add a facility to produce electrical wire from molten aluminum.

Forest products The outbreak of the Northwest's worst forest fires in a half-century — following the region's hottest and driest summer in memory—blackened millions of dollars worth of timberland, idled thousands of loggers, and played havoc with the lumber market from the Pacific to the slopes of the Rockies. Hardest hit were the Cascade Mountains of Washington and Oregon and the Idaho panhandle near the Canadian border. The fires forced the closure of nine national forests at the height of the logging season; this factor, together with a sharp increase in log exports, created a serious shortage of logs which curtailed lumber production throughout late 1967.

Log exports to Japan increased sharply last year to more than 1.5 billion board feet. Industry officials claim that these exports are damaging the log supply available for domestic use and inflating Federal stumpage prices, which have almost doubled since 1962. The major lumber and plywood associations are urging the Federal government to establish a quota of 350 million board-feet of logs available for export each year from public timberlands, so as to relieve the position of small and medium-sized domestic mills that depend on Federal timber supplies.

The pulp and paper industry, although operating at high levels, was faced with the threat of over-capacity last year because of sluggish demand for newspaper and unbleached kraft. Expansion of facilities nonetheless continued during 1967. One major company completed a $60-million expansion program, while a newcomer to the field readied plans to build a $40 million pulp, paper and converting mill near Halsey; another firm will build a new plant in the Yakima area.

Aerospace Employment in the Seattle-Everett-Tacoma area topped 100,000 last year, a new record. Output of the commercially popular model 727 was very strong, and the total backlog of commercial-jet orders exceeded $5 billion at mid-year. This, along with a potential $30-billion market for the SST, assure a high level of production into the next decade. Development costs for the 400-passenger 747 jet transport have already reached $700 million, and a further $150 million will be spent on building the prototype of the supersonic transport.

Defense contracts let to Pacific Northwest firms last year included: $34 million for maintenance and modification of military aircraft and electronic systems; and $49 million for 9 wooden minesweepers for the U.S. Navy.

Steel Construction began in 1967 on a $35-million fully integrated steel-producing complex at the Port of Portland's Rivergate

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Industrial District. The project will eventually include electric-furnace facilities capable of producing 150,000 tons of steel a year (capable of expansion to 500,000 tons a year), rolling-mill facilities for producing large-size steel plates up to 3 inches thick and 96 inches wide, and a plant to produce pre-reduced pellets containing a minimum of 95 percent metallic iron. The new complex will be able to supply the heavy regional demand for large-size plates—a demand which cannot be met by the three steel mills, with an annual capacity of about 700,000 tons, now operating in the Pacific Northwest.

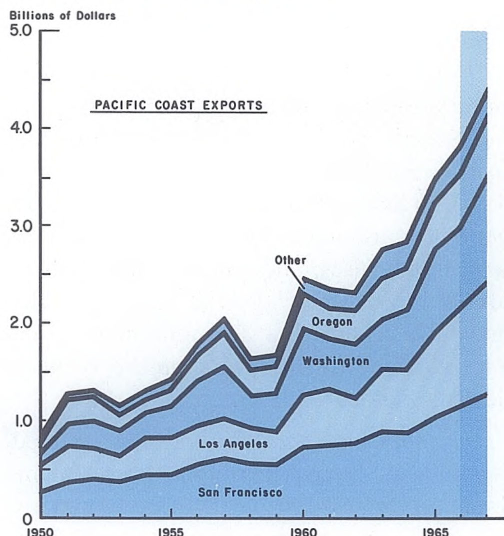
Construction Prosperity has caused strong housing activity in parts of Washington, typified by construction of three high-rise apartments costing $40 million on a 20-acre marina-lagoon site in Haughton. New commercial projects in the area include: $100 million for an industrial-residential-commercial complex to be built over the next 15 years at Lynwood; $30 million for the modernization of Lakewood Industrial Park in Tacoma; and a $15-million shopping center in Eugene.

Utility firms have in the planning stages a $130-million, one-million-kilowatt nuclear-power plant at either Trojan or Beaver, Oregon; a $150-million nuclear-generating plant to be built in Bellingham, Washington; and a $139-million, one-million-kilowatt coal-powered generating station and power transmission lines near Centralia, Washington.

MOUNTAIN STATES

Copper Although the six-month-long copper strike caused a severe decline in output, work continued on projects to expand copper production capacity. The $100-million program initiated in 1963 at the Bingham Canyon property in Utah was completed by mid-year; with the expansion of concentrating and smelting facilities at

Export trade grows rapidly at all West Coast ports



the site, capacity rose from 200,000 to 300,000 tons per year.

The new Twin Buttes open-pit copper mine continued under development twenty miles south of Tucson, Arizona. When completed in 1970, at a cost of $50-$60 million, the mine will have an estimated capacity of 60,000 tons of copper per year.

Another company signed a contract with the General Services Administration to develop a new ore body adjacent to the Esperanza mine in the Twin Buttes mining district, at a total cost of $151 million. When in production, this property will rank with the largest open-pits in the state, having an eventual capacity of 68,000 tons a year. When these and other new properties are completed, total District capacity will rise from 1.1 million tons to over 1.5 million tons.

Silver The increase in the price of silver spurred exploration activity in the Coeur d'Alene region of Idaho. At the Rainbow property, exploration work was scheduled

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

at the 3,475-foot level. At the Galena mine, plans were made to deepen one mine shaft and to increase milling capacity from 500 to 800 tons daily.

Electronics Arizona took on increased importance as an electronics center last year. One electronics firm — the largest single industrial employer in the state, with over 14,000 workers — received major contract awards for armament fuses, electronic equipment, bomb fuses, and guidance and control parts for Sidewinder guided missiles. The Navy also awarded a $16-million contract to an Arizona firm for work on the Walleye television-guided glide bomb.

Petroleum and gas Exploration resulted in significant discoveries of oil pools in the Mountain States last year. One company has already begun producing on the Navajo Indian Reservation in Arizona. In Utah, drilling was productive in the Wasatch Tertiary, in the Redwash area, and at Gregory in the Green River Basin.

Chemicals Large-scale expansion programs were continued by major chemical firms in Arizona and Idaho. One project, at Benson, will increase production of nitric acid from 100 tons to 150 tons per day. Another project, at Kellogg, will double sulphuric-acid output to 215,000 tons a year.

Construction Commercial complexes began to sprout up in many Mountain areas last year. In Nevada, a $320-million project was scheduled near Henderson, Clark County; when completed, it will include a civic center, shopping centers, a 500-room hotel-apartment building, a housing development, and a 360-acre lake development. Las Vegas projects include $80-million and $50-million hotels and a $22-million shopping center. In Arizona, planning got underway for a $40-million housing development, shopping center, motel and golf course at Flagstaff.

Utility companies scheduled work on $30 million of new facilities at Hell's Canyon, Idaho; $40 million for electric and gas installations in Arizona; and $500 million for a coal-burning power plant in the Raiparowits Plateau of Southern Utah. Federal Government spending centered around the $115-million drilling-tunneling-maintenance work at the Atomic Energy Commission's Test Site near Las Vegas, and around a $100-million building program for highways, dams, and other structures in Idaho.

ALASKA AND HAWAII

Petroleum and gas Alaskan oil production jumped by the end of 1967 to over 130,000 barrels a day, mostly from the Swanson River field. Two newly opened fields each reported more than 100 million barrels of oil reserves; in fact, the state's proved reserves have increased from an estimated 700 million to 1,300-million barrels.

A number of major oil firms began full-scale development of a 40,000-acre portion of Alaska's Cook Inlet. Several other major investments were made in petroleum activity, and one firm meanwhile developed a new gas discovery in the Beaver Creek area.

Travel Tourism in Hawaii expanded sharply in 1967 with one million visitors spending an estimated $420 million. This represents a gain of about 40 percent over 1966. The Military Rest and Recuperation Program attracted over 100,000 servicemen and their dependents during the year.

Four new hotels opened during 1967. These included a 288-room and a 525-room hotel in Waikiki, as well as two smaller hotels in Hilo. The number of hotel rooms increased by 1,272 in Waikiki and 1,088 on the neighbor islands. The total has now reached 18,000 hotel rooms, and 4,530 additional are still under construction.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Transport Air travel to Hawaii continued expanding in 1967, with the airlines now carrying 95 percent of all visitors to the Islands. One major airline last year increased its inter-island transportation service for travelers from the mainland. Another airline plans to introduce 350-passenger jumbo-jet service in 1969 with substantially reduced fares — $80 from California and $90 from Seattle-Portland.

In Alaska, air passengers and cargo volume also increased rapidly in 1967. To support this expansion, two major plans have been developed: $7.5 million for cargo-handling facilities and other improvements at Anchorage, and $9.4 million for an airport at Gravina Island, Ketchikan.

Construction Waikiki is still the most popular spot in Hawaii for new hotels and high-rise condominium apartments. The most notable developments announced during the year were a $100-million urban-renewal project for the entire Waikiki area, and a $50-million project for restoration and improvement of the Royal Hawaiian Hotel. In addition, a $180-million resort and residential complex will be built at Kailua-Kona on the Island of Hawaii.

Defense construction in Hawaii rose to a record $600 million in 1967. The Island of Oahu was announced by the U.S. Army Defense Command as one of ten bases for its National Sentinel System (long-range anti-ballistic-missile system) at an estimated installation cost of $100 million. Also, three major utilities announced plans to invest a total of $264 million in plant and equipment during the 1967-71 period. With a view to meeting rising demand for power in the Oahu area, another company has a $100-million, 5-year expansion program that will add one new plant every other year.

In Alaska, the Federal government plans to spend more than $20 million in the next few years to explore the suitability of Amchitka as a site for underground nuclear testing. In the utility field, a $40-million project near Juneau calls for building a 112-ft. dam on Long River with an 8,000-ft-long power tunnel, a 1,400-ft-penstock and a 70,000-kilowatt power plant.

Monthly Review is edited by William Burke. Principal contributors to this issue included: William Burke (U. S. business); Herbert Runyon (fiscal-monetary policy); Ernest Olson (balance of payments); Robert Johnston (credit markets); Verle Johnston (U. S. banking); George Dimmler, Adelle Foley, Verle Johnston, Yvonne Levy, Donald Snodgrass, and Joan Walsh (District business); Ruth Wilson (District banking); Paul Ma, Yvonne Levy and Joan Walsh (District highlights); R. Mansfield (artwork); Donald Alexander (editorial); and Phoebe Fisher (production). *Monthly Review* is published by the Bank's Research Department: J. Howard Craven, Vice President; Gault W. Lynn, Director of Research.

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis

Digitized for FRASER
http://fraser.stlouisfed.org/
Federal Reserve Bank of St. Louis