
FRBSF WEEKLY LETTER

November 18, 1988

The West: Slowing, But Still Strong

As 1988 comes to a close, the economy of the Twelfth Federal Reserve District remains strong. Moreover, current trends suggest that this strength will carry into the next year, although employment growth probably will slow compared to the growth posted in the past several years. In this *Letter*, we discuss the forces causing this slowdown and the implications of slower growth for the major sectors of the Western economy.

A long expansion

Since 1983, the West has enjoyed solid employment growth, averaging 3.5 percent a year. Consequently, the unemployment rate in the District has fallen sharply over this period, from 11.0 percent in January 1983 to 5.5 percent in September 1988.

This low unemployment rate is making it more difficult for employers to find workers to fill new jobs. This puts upward pressure on wages as employers are having to compete for workers. Rising wages caused by the shrinking pool of unemployed workers in the West, in turn, is beginning to exert a restraining force on further employment growth. Ironically, then, the expected slowdown in growth next year is partly due to the strong employment gains made earlier.

Patterns of labor market scarcity help to explain some of the differences among the growth rates anticipated in various parts of the West. Areas that have been growing more rapidly now are reaching constraints on growth. Although the high wages and available jobs in fast-growing areas continue to attract new migrants and help to prolong growth spurts, increases in the costs of labor and real estate eventually force firms to seek areas with slack labor markets. For example, western Washington and the areas around San Francisco and Los Angeles have expanded rapidly in recent years. Now these areas are

imposing limits on further growth, and employers are complaining of labor shortages. As a result, the rate of growth is rising in parts of the West where labor is more plentiful, such as eastern Washington, Idaho, Utah, and central California.

In fact, the pattern of growth in the District in the next several years may well be one of "filling the gaps." That is, areas that have large pools of unemployed workers will become increasingly attractive sites for employers seeking to expand operations. In contrast, the regions that have grown most rapidly in the past will tend to have slower employment growth. Nonetheless, income in both areas should rise; in the formerly slow-growing areas because of employment growth; and in the previously fast-growing areas because the proportion of skilled workers in areas with more developed infrastructure will rise.

Trade and services

Overall trade and service activity in the West should continue to post modest growth, although the volume of domestic retail trade, which is expected to grow by about three percent in 1988, may grow at a slower rate during 1989. At the same time, continued growth in international trade should buoy the financial firms that offer services related to that activity, particularly in the booming port cities of Seattle and Los Angeles. Western banks appear to be headed for healthy profits in 1988, and anticipate another solid year in 1989.

Resource industries

The natural resource industries should play a major role in this process of "filling the gaps." This year's drought generally improved conditions for western farmers working irrigated land, as sharply higher prices have more than offset slightly lower yields. Consequently, the rural economy now is stronger than it has been in several years. Farmers have reduced their debt burdens and land prices are rising. Farm exports

THE WESTERN ECONOMY

The Western Economy is a quarterly review of economic conditions in the Twelfth Federal Reserve District. It is published in the *Weekly Letter* on the third Friday of February, May, August and November.

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have risen, and reduced trade barriers continue to benefit producers of many of the region's crops. However, water supplies currently are severely depleted in many parts of the District, and a continuation of the drought into another year would reverse the gains farmers have made in the last few years.

Most of the region's forest products firms anticipate another profitable year, as continued strength in pulp and paper offsets weakening demand for construction materials. Slowing U.S. construction activity and decreased demand for logs by Japan are reducing demand for lumber and plywood, while increased fire danger and environmental restrictions could limit production.

Mineral mining has strengthened in the West, and continued economic growth should keep demand strong for silver, gold, copper, phosphate, and molybdenum. District-wide mineral mining employment is estimated to have grown almost seven percent during the past year, with Nevada accounting for 36 percent of the net job creation. Nevertheless, recent labor-saving innovations in mineral extraction technology have kept job totals well below the peak levels of the early 1980s. In contrast, the energy production industry remains depressed by low oil prices. If oil prices do not rebound from current levels, oil companies are likely to reduce exploration and development budgets, which could deal a further blow to the Alaskan economy, in particular.

Manufacturing

The outlook for the manufacturing sector remains bright. Manufacturing employment growth in the District has been close to the national pace, as strong demand for computers and commercial aircraft has offset weakness in defense-related products. Slowing national growth is expected to cause a slowdown in electronic components sales; the ratio of orders to shipments has been falling in the semiconductor industry since May,

but the level of activity remains high. The aerospace industry has suffered somewhat from the drop in defense expenditures, but strong demand for commercial aircraft has helped to buoy the industry. Boeing and McDonnell Douglas, based in Seattle and Los Angeles, respectively, together produce more than 85 percent of the nation's commercial aircraft, and both firms report growing waiting lists for new aircraft.

Construction and real estate

The construction outlook reflects the broad trends in the region. Construction is strong in Washington and California, where recent employment and population growth have increased the demand for residential structures. Real estate values have risen sharply in most of the region's major cities, causing problems of affordability that threaten further employment growth in those areas. Real estate prices also are rising in Oregon as a consequence of its recent economic improvement.

In Idaho, road building and commercial construction are spreading through the state, signalling a possible broadening of economic expansion to the more rural areas. Construction remains weak in Utah, despite recent gains in employment, since vacancy rates remain high.

Alaska and Arizona both suffered from extremely slow construction activity this past year, and a turnaround will take time. The stock of surplus housing will keep the market in Alaska depressed. Likewise, the Arizona market is overbuilt, given the recent slowdown in population and economic growth. Finally, the spectacularly strong construction activity in Nevada is not likely to be sustained, so some slowdown is likely there as well.

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DISTRICT INDICATORS
(SEASONALLY ADJUSTED)

	88Q3	88Q2	88Q1	87Q4	87Q3	87Q2	87Q1	86Q4	% CHANGE FROM:	
									88Q2	87Q3
AGRICULTURE										
U.S. CROP PRICES, 1985=100	110.6	104.1	102.5	100.6	99.0	99.3	95.6	95.5	6.32	11.75
DISTRICT CROP PRICES, 1985=100	112.4	93.2	98.2	103.0	99.7	102.2	97.9	91.8	20.60	12.77
FARM CASH RECEIPTS, MILLION \$	N/A	2190.1	2336.4	2182.9	2129.0	2111.9	2059.4	2005.2	N/A	N/A
CATTLE ON FEED, 1985=100	96.4	95.8	94.2	95.1	94.0	85.2	82.6	81.0	0.68	2.58
CATTLE PRICES, CALIFORNIA, \$/CWT.	61.8	63.4	61.6	57.8	58.0	56.4	52.4	49.4	-2.47	6.61
FORESTRY										
LUMBER PRODUCTION, MILLIONS BOARD FEET	1508.6	1647.5	1718.1	1661.9	1687.1	1756.1	1806.5	1822.0	-8.43	-10.58
NORTHWEST LUMBER INVENTORY, MIL. BOARD FEET	2459.7	2498.3	2509.1	2478.4	2606.7	2637.6	2581.1	2608.8	-1.55	-5.64
U.S. LUMBER PRICES, 1985=100	113.8	113.4	110.6	109.4	61.1	33.3	32.4	31.6	0.36	86.31
ENERGY										
SPOT PRICE OF OIL, \$/BARREL	15.5	17.3	16.7	18.7	20.4	19.3	18.2	15.3	-10.34	-23.94
U.S. RIG COUNT	957.8	1061.7	973.8	1002.2	1037.5	880.0	810.5	786.9	-9.78	-7.68
DISTRICT RIG COUNT	93.4	96.9	79.1	99.5	102.9	82.6	60.1	61.8	-3.60	-9.23
FUEL MINING EMPLOYMENT, 1985=100	78.8	79.3	77.2	77.9	78.2	77.6	76.0	77.1	-0.69	0.69
U.S. SEISMIC CREW COUNT	187.0	201.9	199.1	189.8	181.9	173.8	157.5	152.3	-7.40	2.81
MINING										
MINERAL PRICES, 1985=100	148.6	153.1	152.7	147.4	130.0	120.0	106.9	103.7	-2.96	14.30
METAL MINING EMPLOYMENT, 1985=100	156.7	148.8	141.4	131.8	126.8	119.7	111.7	102.6	5.34	23.62
CONSTRUCTION										
NONRESIDENTIAL AWARDS, MILLION \$	1571.9	1325.0	1481.9	1599.2	1476.1	1504.2	1450.6	1405.4	18.63	6.49
RESIDENTIAL PERMITS	32725	30907	27923	28694	30783	30200	32517	41469	5.88	6.31
WESTERN HOUSING STARTS, THOUSANDS	36.7	36.8	28.5	27.9	37.6	40.1	34.3	35.5	-0.18	-2.31
CONSTRUCTION EMPLOYMENT, THOUSANDS	970.3	957.7	945.6	916.9	909.9	905.8	901.3	895.6	1.31	6.64
MANUFACTURING										
WAGES, CALIFORNIA, \$/HOUR	10.9	10.8	10.8	10.9	10.8	10.7	10.6	10.5	0.77	0.77
EMPLOYMENT, THOUSANDS	3082.8	3086.1	3086.4	3056.1	3024.7	3004.1	2991.1	2982.7	-0.11	1.92
DURABLES, 1985=100	102.2	102.1	102.2	101.1	100.4	99.7	99.3	99.1	0.06	1.75
CONSTRUCTION DURABLES, 1985=100	108.1	109.7	110.8	108.4	107.6	107.4	107.1	105.9	-1.45	0.46
AEROSPACE, 1985=100	115.9	115.6	115.9	114.7	113.4	112.2	111.1	109.5	0.25	2.22
ELECTRONICS, 1985=100	100.1	98.5	98.0	97.2	95.9	94.9	94.7	94.6	1.62	4.32
SEMICONDUCTOR ORDERS, MILLIONS, NOT S.A.	1222.0	1269.0	1126.2	1056.8	967.3	980.7	912.4	757.5	-3.70	26.33
WHLS/RETAIL TRADE EMPLOYMENT, THOUSANDS	4542.9	4495.5	4462.2	4383.9	4347.1	4306.4	4259.6	4234.3	1.06	4.50
RETAIL SALES, PACIFIC DISTRICT, MIL. \$	20583	20559	20615	20133	19722	19531	18947	19015	0.12	4.37
SERVICES EMPLOYMENT, THOUSANDS										
HEALTH CARE, 1985=100	114.5	113.4	112.7	111.4	110.1	108.7	107.7	106.0	0.92	3.99
BUSINESS SERVICES, 1985=100	120.5	119.2	118.6	115.9	115.1	113.5	111.3	109.2	1.09	4.71
HOTEL, 1985=100	119.2	117.0	116.3	114.9	112.2	110.6	108.8	106.4	1.87	6.22
RECREATION, 1985=100	107.3	108.2	109.3	108.2	106.1	106.6	105.4	103.3	-0.81	1.14
FINANCE, INSUR. AND REAL ESTATE EMPLOYMENT										
	1222.4	1214.7	1215.8	1209.2	1204.5	1196.2	1182.6	1169.2	0.64	1.49
GOVERNMENT EMPLOYMENT, THOUSANDS										
FEDERAL GOVERNMENT	607.5	606.1	610.3	609.9	605.3	605.2	601.0	599.5	0.22	0.36
STATE AND LOCAL	2618.1	2598.0	2570.1	2551.1	2527.3	2502.3	2490.0	2479.4	0.77	3.59

Data are weighted aggregates of available 12th District state data and are expressed as monthly rates unless otherwise noted. District Indicator data are constructed by FRBSF research staff from public and industry sources.

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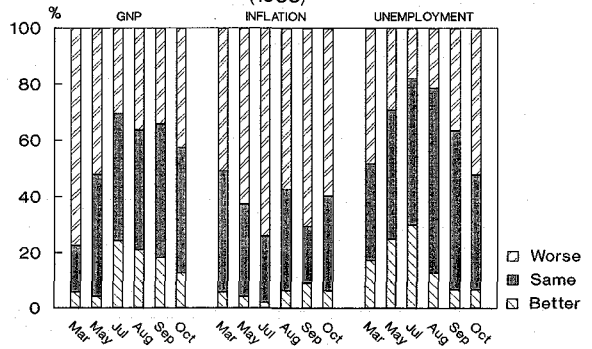
Research Department
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Alaska Arizona California Hawaii Idaho
 Nevada Oregon Utah Washington

PERSONAL INCOME
 ANNUALIZED PERCENT GROWTH RATES

	88Q2	88Q1	87Q4	87Q3	87Q2	ANNUAL GROWTH		
						1988	1987	1986
ALASKA	4.4	2.3	2.4	0.1	6.2	3.4	-0.6	-1.4
ARIZONA	10.3	-4.0	14.0	6.2	9.4	2.9	9.2	9.1
CALIFORNIA	10.5	1.0	12.2	6.5	10.2	5.7	9.5	7.5
HAWAII	9.1	7.5	13.5	9.2	8.6	8.3	9.7	7.9
IDAHO	10.1	10.9	-0.2	5.4	10.5	10.5	4.5	3.9
NEVADA	12.7	6.4	13.7	12.2	11.1	9.5	11.8	9.0
OREGON	7.8	7.3	8.7	6.7	9.4	7.6	7.6	5.8
UTAH	11.3	-0.3	9.3	3.4	9.4	5.3	6.6	3.3
WASHINGTON	7.8	8.9	10.3	5.5	7.7	8.3	5.9	8.8
12TH DISTRICT	10.0	2.1	11.6	6.4	9.8	6.0	8.8	7.4
U.S.	7.4	4.6	11.6	7.1	6.7	6.0	8.5	5.9

Twelfth District Business Sentiment Index*
 (1988)



* The index is constructed from a survey of approximately 75 business leaders in the 12th Federal Reserve District.

NON-AGRICULTURAL EMPLOYMENT
 ANNUALIZED PERCENT GROWTH RATES

	88Q3	88Q2	88Q1	87Q4	87Q3	ANNUAL GROWTH		
						1988	1987	1986
ALASKA	-1.8	-5.8	1.4	4.9	-4.6	-2.1	-1.7	-6.4
ARIZONA	-0.2	-1.9	3.4	4.0	3.0	0.4	3.1	4.1
CALIFORNIA	3.1	2.5	5.3	3.3	3.5	3.7	3.6	2.5
HAWAII	1.5	1.6	4.7	7.4	1.9	2.6	3.8	2.6
IDAHO	1.6	1.0	4.4	3.2	2.9	2.4	1.0	-0.2
NEVADA	6.4	2.2	7.5	7.0	5.9	5.4	6.7	5.8
OREGON	4.4	0.9	6.9	3.8	2.8	4.1	3.5	2.7
UTAH	3.8	4.0	0.8	2.8	-0.4	2.9	1.3	1.0
WASHINGTON	3.7	3.7	4.8	5.4	4.2	4.1	4.5	3.6
12TH DISTRICT	3.0	2.1	5.0	3.8	3.3	3.4	3.5	2.6
U.S.	3.3	3.6	3.8	4.0	3.3	3.6	3.3	2.0

UNEMPLOYMENT RATES
 AVERAGE QUARTERLY DATA

	88Q3	88Q2	88Q1	87Q4	87Q3	ANNUAL AVG.		
						1988	1987	1986
ALASKA	8.8	8.9	9.3	10.1	10.6	9.0	10.8	10.9
ARIZONA	6.5	5.7	5.6	6.0	6.1	5.9	6.3	6.9
CALIFORNIA	5.4	5.7	5.2	5.4	5.5	5.4	5.7	6.7
HAWAII	3.0	2.9	3.5	3.8	3.8	3.1	4.0	4.9
IDAHO	5.5	6.3	7.4	7.3	7.4	6.4	8.0	8.8
NEVADA	5.3	5.7	6.0	6.0	6.3	5.7	6.3	6.0
OREGON	6.1	6.1	6.0	5.7	5.8	6.0	6.2	8.5
UTAH	4.7	5.0	5.5	5.9	6.4	5.1	6.4	6.0
WASHINGTON	6.6	6.6	7.0	7.4	7.4	6.7	7.6	8.2
12TH DISTRICT	5.6	5.8	5.5	5.8	5.9	5.6	6.1	7.0
U.S.	5.5	5.4	5.7	5.9	6.0	5.5	6.2	7.0