

Tennessee: Continuing the Momentum of Recovery

Business cycle trends make the outlook for Tennessee's economy brighter than in several years, but such structural factors as the balance of manufacturing and service employment will influence the degree of improvement felt in different regions of the state. Certain sectors, such as construction and consumer spending which typically lead the expansion during the early phases of recovery, already have experienced a strong rebound in Tennessee and in the nation. Building-related manufacturing also has registered substantial employment gains.

Industries that tend to trail the initial recovery because they are oriented to demand from capital investment should experience more improvement in 1984. Since capacity utilization had fallen to low levels during the recession, many employers were able to increase output in the early phase of recovery without adding plants or equipment. A rise in the utilization rate reported by the Federal Reserve Board from 70.1 percent in November 1982 to 79.2 percent in November 1983 and sharp increases in U. S. corporate profits foretell substantial expansion of plants and equipment, thereby boosting demand for Tennessee's basic and intermediate industries.

The state's unemployment rate, which remained in the double-digit range through November, should fall in 1984 because of cyclical dynamics. During early phases of recovery the labor force typically increases as formerly discouraged workers reenter the labor market in search of jobs. However, employers, still cautious, tend to increase hours of employees already on their staffs before hiring new workers. A rise in average weekly hours in Tennessee from 39.5 in November 1982 to nearly 41 by last November suggests employment growth on the horizon.

Continuation of recovery may stimulate exports as foreign economies begin to strengthen. In addition, demand for exports could grow if the foreign exchange rate of the dollar declines from its



Tennessee's interest-rate sensitive industries bounced back well in 1983, but the state's continuing dependence on manufacturing poses structural problems for the near future.

current level, 30 percent higher on a trade-weighted basis with major trading partners than it was three years ago. Increased exports would boost Tennessee's agricultural and manufacturing sectors. Exports are unlikely to increase sharply, though.

Finally, state and local government spending should increase, providing an additional stimulus. The effect of recovery on government revenues came too late to be reflected in fiscal year 1984 budgets, prepared in the spring, but should be in evidence by the third quarter of 1984. Although expansion of the housing industry may slow as the recovery matures, general increases in employment and growth in commercial construction and industries that have yet to improve should maintain a strong momentum. An Atlanta Fed poll of Tennessee businesses in late 1983 revealed considerable optimism for 1984.

Structural Factors

Nonetheless, the state's continuing dependence on manufacturing poses structural problems that may slow Tennessee's return to prerecession peaks. Manufacturing accounts for 27 percent of Tennessee's nonfarm jobs but only 22 percent of the nation's, despite the rapid growth of service jobs in Tennessee over the last decade. From 1971 to 1982, Tennessee gained 56,000 jobs in health care, 18,000 in miscellaneous business services, and 37,000 in restaurants, compared with a net gain of 18,000 nondurable manufacturing jobs and 40,000 durable manufacturing jobs.¹ Similarly, while the share of personal income attributable to nondurable manufacturing declined by one percentage point, miscellaneous services' share rose by two.²

Moreover, Tennessee's manufacturing base is concentrated in labor-and energy-intensive industries that may be undergoing secular declines. These will not be reversed by the present recovery. Over the last decade pressures from lower-cost foreign producers have whittled employment in apparel and chemical manufacturing, Tennessee's largest industries in terms of jobs. Increasing power costs in the 1970s denied Tennessee's energy-intensive industries, such as aluminum and pulp and paper, one cost

advantage that had brought them to the state initially.

Related changes in the energy sector exacerbated another structural problem in Tennessee manufacturing: its concentration in credit-sensitive durable goods, especially those tied to construction and transportation. During the 1970s, the Tennessee Valley Authority's (TVA's) nuclear power plant construction engendered rapid growth that offset the volatility of durable goods employment and helped keep Tennessee's unemployment rate below the nation's. Termination of this expansion program over the past few years has removed an important buffer, and as in the 1960s, the state's unemployment rate is higher than the nation's.

Tennessee has shown signs of strength in attracting more diversified business and industry with higher profit, less cyclical products. Tennessee ranked 13th in a rating of state manufacturing business climates; six of its southeastern neighbors ranked higher, though.³ The state's high ranking on a national scale was influenced by its relatively low taxes and wages and its formerly rapid population growth. Weaknesses included high energy costs, frequency of work stoppages, and a comparatively low percentage of high school educated adults. A recent poll of the nation's 30 largest cities indicates that Nashville and Memphis have the second and third lowest residential utility rates, but industrial rates are no longer relatively cheap.⁴

The potential for diversification to more profitable kinds of manufacturing has begun to be realized. An estimated 85 advanced technology firms with 30,000 workers operate in the Oak Ridge/Knoxville area of East Tennessee. Government installations, such as the Oak Ridge National Laboratory, two other Department of Energy (DOE) facilities involved in uranium enrichment for nuclear plants and nuclear weapons production, the University of Tennessee, and the TVA, form the bulk of the state's high-technology base. The product strengths of this area include energy systems, instrumentation, measurement, and biotechnology.

The growing technological influence on Tennessee manufacturing is found in the private

¹U.S. Department of Commerce, **County Business Patterns**, Tennessee, 1971, p. 11, and p. 1 of the 1981 issue.

²Computed from data in State Survey Tables, Bureau of Economic Analysis, U. S. Department of Commerce (not published).

³The Fourth Study of General Manufacturing Business Climates of the 48 Contiguous States of America, Alexander Grant and Company, 1983, p. 4.

⁴"Cost of Electricity in Major Cities Compared," **Public Power** (November-December 1983), pp. 22-24.

sector as well. Tennessee Eastman has spent more than \$500 million on a coal gasification project that will convert coal into chemical building blocks used to make photographic film, plastics, cigarette filters, and synthetic textiles among other products. This project was tested last fall and is scheduled to be fully operational early this year. In addition, Tennessee is a leader in the Southeast in Japanese investment. More than 20 Japanese companies have invested over \$1 billion in the state. The largest, Nissan, is pioneering in the application of modern management techniques to traditional industry. Nissan's newly opened plant south of Nashville is a model of congenial labor-management relations. The emphasis on shared responsibilities for quality products and the utilization of advanced technologies make this plant a paradigm of the attributes some analysts believe are necessary to restore America's industrial prominence.

Although these examples imply future strength in large manufacturing operations, the future for small businesses appears less bright. Tennessee ranked 24th among states' climates for small businesses. Low ratings in capital resources, labor, and general business activity (population, employment, and personal income growth) offset the effect of the state's low tax structure. The state has a loan-to-asset ratio below the median of 51.6 percent and lacks a state-sponsored venture capital program.⁵ These factors could deter the growth of private high technology firms and other small businesses.

Sharp Geographic Differences

A noteworthy structural factor pertains to geography. Statewide averages and even SMSA data often overlook the typical experiences of the majority of Tennesseans who live in smaller cities and rural areas. Only 45 percent of Tennessee's 4.6 million residents live in cities of 50,000 or more, and 40 percent live in rural areas of fewer than 2,500 people. Only 26 percent of Americans live in such areas.⁶ Moreover, Tennessee has three regions, with distinct economic as well as cultural and political traditions that will help determine the course of

developments in 1984. West Tennessee accounts for 27 percent of the state's population. Per capita income there averaged \$9,232 in 1981 (see map). Middle Tennessee had 31 percent of the state's population and average per capita personal income of \$8,970. East Tennessee had 39 percent of the population; per capita income averaged \$8,070.⁷

West Tennessee's economy is based largely on agriculture, especially soybeans and other food crops, which have proven as amenable to extensive cultivation in the plateau extending from the Tennessee River to the Mississippi as cotton once was (see map). Farm cash receipts exceeded \$30 million in five of west Tennessee's 21 counties; only one of Tennessee's other 74 counties enjoyed such a high dollar volume of agricultural products.⁸ Memphis has long been a trade and transportation center for farm products from Tennessee and neighboring states. As shown in Table 1, Memphis continues to depend more on services than on manufacturing. The concentration ratios in this table measure under- and over-representation of various sectors in Tennessee cities. Memphis's concentration ratio of 1.54 for transportation indicates its share of jobs in this sector is more than 50 percent greater than its overall share of the state's jobs. However, the city's meager 2 percent projected population growth for the 1980s portends slow growth in construction, retail trade and other services. The State Planning Office conservatively projects population growth of 8-19 percent in other Tennessee SMSAs.

In east Tennessee, mountainous terrain makes farming difficult, but burley tobacco is an important cash crop. However, the mountains' abundant natural resources have led to a concentration of durable goods manufacturing and heavy industry. Coal in northeastern Tennessee attracted heavy industry after the Civil War and still provides energy supplies to the TVA. This mountainous area's extensive hardwoods drew Tennessee Eastman, DuPont, and other chemical manufacturers there half a century ago to convert cellulose and other lumber products into chemicals needed by industry and consumers. The region's abundance of

⁵ Inc. (October 1983), pp. 140ff.

⁶ Population Characteristics, Series P-20, No. 374, U. S. Department of Commerce, Bureau of the Census (September 1982), p. 12.

⁷ Computed from data in U. S. Department of Commerce, Bureau of Economic Analysis, Local Area Personal Income, 1976-81, Southeast

Region (June 1983), pp. 246-271. (Percentages do not add to 100 because of rounding.)

⁸ U. S. Department of Commerce, Bureau of Census, 1978 Census of Agriculture, Tennessee (April 1981), p. XVI.

Table 1. Tennessee SMSA Concentration Ratios

SMSA	Goods		Services				Total Services	
	Const.	Manu.	TCPU	FIRE	Trade	Misc. Serv.		
Chattanooga	0.84	0.97	0.93	1.28	0.99	0.95	1.09	1.01
Knoxville	1.10	0.87	0.81	0.90	1.02	0.98	1.25	1.05
Memphis	0.82	0.57	1.54	1.18	1.26	1.21	1.02	1.20
Nashville	1.19	0.77	1.08	1.46	1.09	1.14	0.94	1.10

Source: Computed from data in U.S. Dept. of Labor, Bureau of Labor Statistics, **Employment and Earnings**, May 1983, pp. 122-123.

zinc and pyrites used to make sulfuric acid helps Tennessee lead the United States in production of these minerals.⁹

The institution of the TVA in the 1930s made cheap energy readily available, and public officials encouraged energy-intensive industries such as aluminum to locate in the area. Yet the future of many east Tennessee industries is clouded by the rapid growth in energy costs in recent years and foreign competition. Moreover, east Tennessee's major cities, Knoxville and Chattanooga, have been slow in the transition to services (see Table 1). Consequently, the recessions effects were more devastating and current growth is from a lower relative base as seen in higher unemployment rates (see map).

In middle Tennessee the rolling terrain of the Cumberland Plateau lends itself to a more diversified economy. Livestock complements food and tobacco crops in importance in rural areas. Nashville has become a service center (see Table 1), offering not only distributive services (trade and transportation) like Memphis but also many business and consumer services, such as health care, insurance, private education, and finance. Moreover, the largest local source of manufacturing jobs, printing and publishing (see Chart 1), involves the dissemination of information, which many analysts consider the underlying cause of services sector growth.

One sign of the city's prosperity is its booming commercial construction and its ability to fill new office space relatively quickly. Nonetheless, middle Tennessee has pockets of poverty and unemployment, particularly in certain rural counties that have relied on a few manufacturing firms to sustain local employment and trade.

General Business and Labor Conditions

New incorporations through the first half of 1983 were 7 percent ahead of 1982.¹⁰ Bankruptcies declined 12 percent in the 17-county area of southeastern Tennessee including Chattanooga during the first 11 months. Bankruptcies declined 11 percent in the Nashville district and 7 percent in the Memphis district. However, in the 24-county area of northeast Tennessee including Knoxville, bankruptcies were nearly on a par with the 1982 level.¹¹

Improvement in labor market conditions was more belated.¹² After falling 2.1 percent in 1982, nonfarm employment statewide began increasing in late 1983, and by November reached 1.7 million, or 3 percent more than the year before but 72,000 less than in 1979. Jobless Tennesseans numbered 34,000 fewer in late 1983 than late 1982, but the labor force grew more rapidly than employment. By November

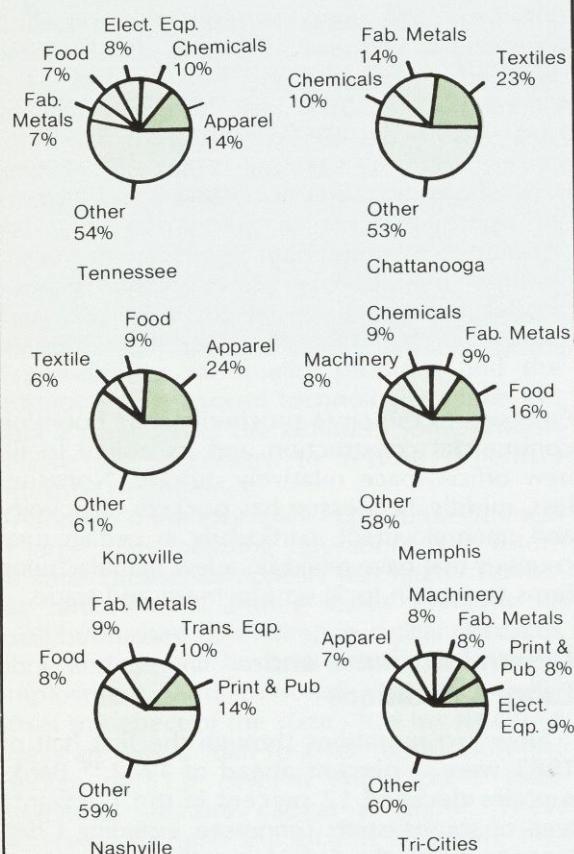
Minerals Yearbook, Vol. II (Washington, D. C.: Bureau of Mines, U. S. Department of the Interior, 1983), pp. 457-469.

¹⁰Computed from data in Dun and Bradstreet, **Monthly New Incorporations**.

¹¹U. S. Bankruptcy Courts of Chattanooga, Knoxville, Memphis, and Nashville.

¹²Changes in the labor market were computed from data published by the Tennessee Department of Employment Security. Unless otherwise indicated, data are preliminary and not seasonally adjusted and changes are relative to year-earlier levels.

Chart 1. Distribution of Manufacturing Employment by Largest Industries



Source: Computed from data in Annual Survey of Manufactures
Bureau of the Census

the percentage of Tennesseans out of work had declined to 11.4 percent (seasonally adjusted) from a peak of 12.8 percent in February 1983, whereas the U.S. rate had fallen to 8.4 percent by that time.

In east Tennessee, labor market conditions remained depressed throughout most of 1983. Chattanooga's employment stood at 166,000 in October, 7,600 fewer than in 1979 and only 2 percent more than in October 1982. However, unemployment began falling relative to year earlier levels in May and by November had reached 9.1 percent. Knoxville had fewer employed through the first three quarters of 1983, and the unemployment rate remained in double-digits through the first half. In contrast, the

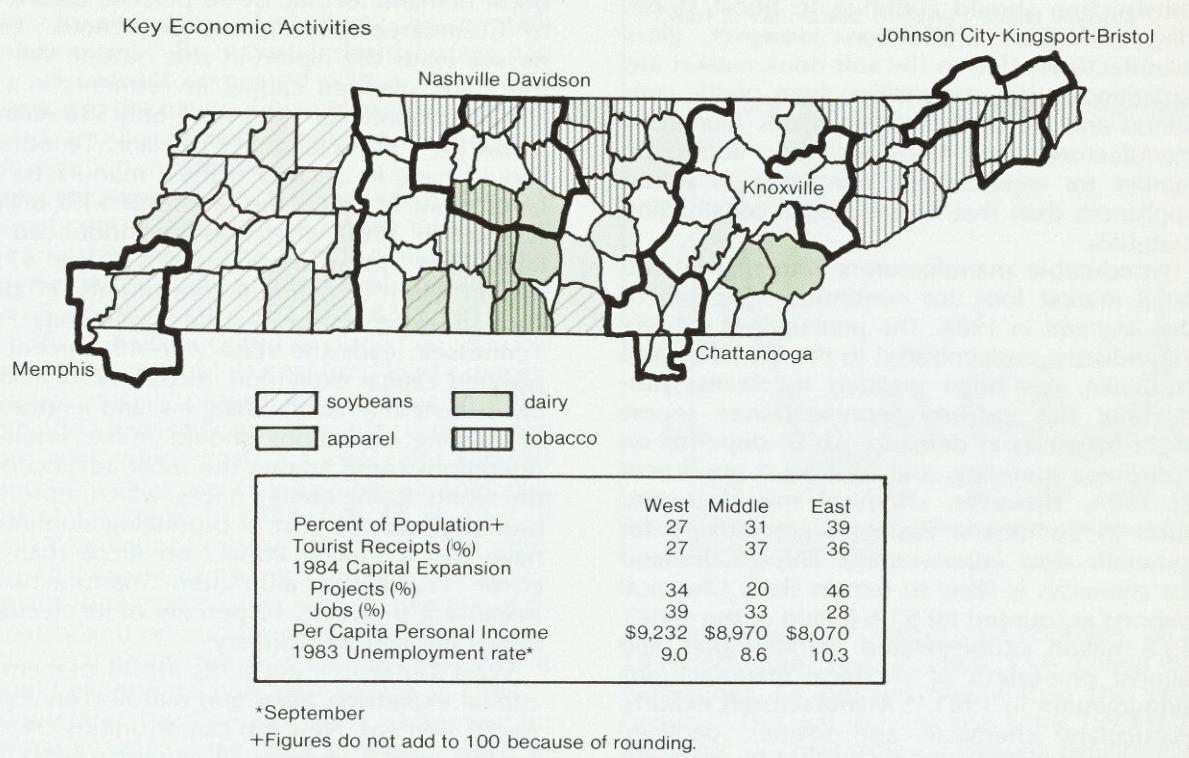
World's Fair helped hold the 1982 unemployment rate at 8.8 percent. Tri-Cities had the highest jobless rate, 9.3 percent, in October. The unemployment rate for East Tennessee as a whole was 10.3 percent in September (see map). Memphis continued to lose jobs through the first nine months, with 347,000 employed there by October. However, the unemployment rate began dropping in June. West Tennessee's unemployment rate was 9 percent in September. In Nashville employment declined by small margins through the first 10 months of 1983, and the 368,000 employed there in October numbered 10,000 fewer than in 1981. However, Nashville's unemployment rate was only 6.9 percent in November. Middle Tennessee's jobless rate was the lowest of the three regions.

The apparent paradox between employment gains statewide and losses in the cities is attributable to the concentration of manufacturing which experienced the largest growth in jobs, outside urban areas. More than half the work force in 23 non-SMSA counties is employed in manufacturing. The labor market outlook for 1984 is positive, but the rate of improvement will vary from one sector of the economy to another.

Manufacturing

Manufacturing employment has been edging higher since mid-1983 and by November had generated nearly 29,000 more jobs than a year earlier. Durable manufacturing improved more robustly than nondurable manufacturing. By November the rate of increase in durable goods employment reached 10 percent, but that in nondurable goods had advanced only 4 percent. Durables added over 19,000 jobs to reach a total of 215,000, whereas nondurables added 9,000 jobs to reach 270,000. Durables and nondurables employment remains below historical peaks of 1979 and 1973, respectively.

The strong recovery in housing and in replacement purchases of household durables stimulated building-related industries. Stone, clay, and glass employment led the growth with a November increase of 25 percent. Lumber and wood employment was up almost 8 percent. These high growth rates in part reflect the low levels to which these industries fell in 1982—the lowest in over a decade. Machinery employment declined through June but rose 11 percent in November. Refrigeration equipment



accounts for 35 percent of nonelectrical machinery employment and value-added, and household appliances, TVs, and radios account for over 40 percent of electrical machinery jobs and value-added.¹³ In response to growing nationwide auto sales, transportation equipment (automobiles and parts) employment began to rise in midyear and by November was 14 percent ahead of last year. Primary and fabricated metals production began to recover later in the summer, achieving 8 and 2 percent respective advances in jobs by November.

Because of lingering weaknesses in the paper, chemicals, and food industries, nondurable manufacturing employment growth was sluggish. In the paper industry employment declines were in the double-digit range in most of 1983. Jobs in chemicals fell throughout 1983 although the rate of decline narrowed in each successive month except August. Chemical manufacturing

accounts for a larger share of value-added (17 percent) than any other industry and ranks second in the share of industrial jobs (10 percent) (see Chart 1). Apparel and textiles employment began to increase last spring and by November had achieved growth rates of 8 and 7 percent, respectively, after declining substantially in 1982. The growth in apparel employment to 69,000 is significant because in terms of jobs it is the largest industry (see Chart 1). Apparel factories are the leading source of employment in 21 of the 39 counties for which such data are available. Textile producers began to recover in 1983 because of increasing demand for apparel, carpets, and auto upholstery.

A poll of Tennessee businesses revealed considerable optimism about the outlook for durable goods manufacturing in 1984. Transportation equipment production should continue to improve in 1984 because Detroit automakers have scheduled a substantial increase in auto assemblies. Growth in lumber industry orders and employment may slow in concert with an expected deceleration in home-building, but the normal three-to-six month lag in commercial

¹³Computed from data in 1978-79 **Annual Survey of Manufactures**, Tennessee U. S. Department of Commerce, Bureau of the Census (January 1983), Section 6, pp. 243-7.

construction should continue to boost stone, clay, and glass production. However, glass manufacturers tied to the soft drink market are experiencing stiff competition from plastic containers and are contemplating layoffs. Aluminum manufacturers are more optimistic about the market for replacement purchases of home appliances than that for residential construction materials.

Nondurable manufacturers who rely on the retail market look for continued increases in that segment in 1984. The printing and publishing industry, concentrated in the Tri-Cities and Nashville, has been plagued by excess production, but industry representatives report slight increases in demand, which depends on consumer spending and forecast a good year in 1984. However, chemical manufacturers, such as Tennessee Eastman, are looking for generally slow improvement. Foreign demand for chemicals is likely to remain slack. Chemical exports accounted for \$1.6 billion of the state's \$5.6 billion export-related manufactures and almost one-fourth of chemical manufacturing employment in 1981.¹⁴ Manufactured exports, particularly chemicals and textiles, declined sharply in 1982 and 1983. Demand for chemicals may not strengthen substantially in 1984 because, even if the exchange rate of the dollar declines, exports normally respond slowly. Moreover, almost 40 percent of Tennessee's chemical production supplies synthetic fibers to textile producers; thus, it is subject to the same long-term constraints as that industry.

Developments in the chemical industry will have a greater effect on Chattanooga and Memphis than on other cities. Chemical production, which accounts for 18 percent of the value added by manufacturing and 10 percent of industrial jobs in Chattanooga, ranks among the top three local industries in a city heavily dependent on manufacturing (see Chart 1). In Memphis, only food outranks chemicals in terms of jobs or the share of value added by manufacturing, but manufacturing comprises a smaller portion of the local economy.

One positive sign for manufacturing is the extent of capital expansions on the horizon. Increased capital spending nationally should

boost demand for zinc by 38 percent, according to Commerce Department projections. Tennessee leads the nation in zinc output. Within the state, planned capital investments in the first nine months of 1983 were only \$36 million below the 1982 total of \$761 million. Tennessee should have its second highest manufacturing investment in 1983; the record of \$1.8 billion was set in 1980 when Nissan announced its half-billion dollar investment. Of the \$725 million worth of planned investments, 77 percent are expansions of existing operations. East Tennessee leads the state with 46 percent of planned capital expansion. Alcoa's \$250 million investment in a new finishing mill and renovation of existing operations should make smelting operations there among the most advanced in the world. Rising energy prices, which represent one-fourth of the cost of producing aluminum, have had a smaller impact on Alcoa than on other Tennessee aluminum manufacturers because it produces 40 percent of its electrical needs through a subsidiary.

West Tennessee accounts for 34 percent of capital expansion plans and middle Tennessee for 20 percent. New job opportunities created by this capital investment should surpass last year's level by 13 percent. Potential new jobs totaled more than 12,000 through September 1983 compared to the 1982 annual level of 10,000. Although east Tennessee will garner the largest share of capital investment, its proportion of job opportunities from this investment are least, comprising only 28 percent of the state's total. West Tennessee's capital investment accounts for 39 percent of the new jobs, and middle Tennessee's accounts for 33 percent.¹⁵

Energy

Tennessee's recovery is reflected in changes in demand for electrical power in 1983. By August, kilowatt hours increased 6 percent in Tennessee, although U.S. usage had climbed 9 percent. However, aggregate demand is well below peak 1979 levels. The revival of Tennessee's industries, especially durable goods, should spark continuing upturn in demand. This trend

¹⁴"Origin of Exports of Manufactured Products." **1981 Annual Survey of Manufactures** (May 1983), pp. 16, 29.

¹⁵Third quarter 1983 Economic Growth Report, Tennessee Department of Economic and Community Development.

is significant because industrial customers account for almost half of all energy consumption in Tennessee.¹⁶ By August, industrial usage had risen 8 percent compared with a 10 percent increase in the nation. Consumer-generated demand should remain moderate because of conservation measures.

On the supply side, the outlook is for continued contraction but at a slower rate than in the past few years. The TVA, the major energy supplier in the state, reduced coal consumption by 4.5 percent from 1982 to 1983. From 1981 to 1983, the utility closed or placed on seasonal status 17 percent of its coal-fired load capacity. Agency officials project little change in 1984 from 1983 levels because the utility is converting from coal, which costs 2.3 cents per kilowatt hour, to nuclear power, which has an operating cost of 1.4 cents. In 1983, fully 55 percent of the TVA's capacity came from coal-fired units and 18 percent came from nuclear; ultimately, it plans to rely on coal for only 47 percent of its capacity and on nuclear energy for 30 percent. Thus, coal production and mining employment should experience only slow growth in 1984.

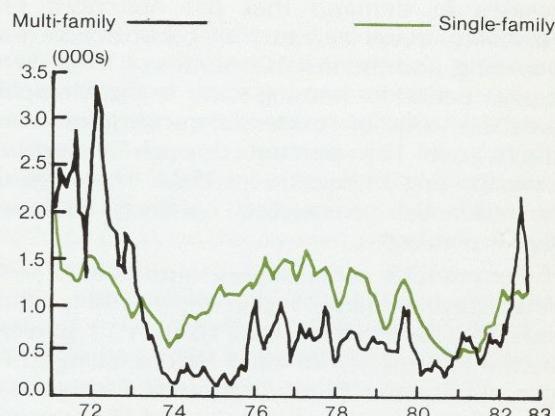
Moreover, the TVA has been attempting for several years to bring capacity more closely in line with demand by cancelling plans for nuclear power plants. Congress terminated funding for the Clinch River breeder reactor, near Oak Ridge, in November. The TVA plans to spend \$1.3 billion on power-generating projects in fiscal 1984, \$300 million less than in fiscal 1983. TVA employment, already reduced from a regional total of 52,000 in 1980 to 37,000 in late 1983, should continue to decline by 4,000 over the next five years albeit at a rate set largely by attrition rather than layoffs. The impact will continue to be greatest in east Tennessee, where two of the six coal-fired plants affected by the shift to nuclear power are located. Of the 24,000 TVA employees in Tennessee, Chattanooga and Knoxville each has around 5,000. Coal mining is concentrated in upper East Tennessee.

Construction

The building industry led other sectors of the state's economy in recovering from the recession.

¹⁶U. S. Department of Energy, **State Energy Data Report**, 1980 through 1980, (July 1982), p. xi.

Chart 2. Tennessee Building Permits 3-Month Moving Average, S.A.



Source: Seasonally adjusted by Federal Reserve Bank of Atlanta from Bureau of Census data.

The dollar value of construction contracts, on a 12-month rate, had reached \$3.6 billion by November, 44 percent higher than the year before.¹⁷ This was the first year since 1979 that the value of construction increased significantly. Residential construction, which comprises half the value of construction spending, led this growth. Single-family building permits doubled in the summer after declining since 1978 and remaining flat in 1982 (see Chart 2); multifamily permits were up 125 percent in November. These rates surpassed those of Georgia and Florida, which did not decline so sharply in the recession. Nonresidential building permits, which did not begin to recover until mid-1983, were 24 percent above 1982 levels by November. In this category, office buildings and stores showed the most strength.

Chattanooga's residential building has been reviving. By November, single-and multifamily building permits had risen over 65 percent (12-month rate) from 1982 levels. The value of nonresidential construction grew at a slower rate, attaining a 49 percent increase through November. Knoxville's growth has been tempered by multifamily permits, which declined almost 60 percent below 1982 levels. The

¹⁷Construction figures were obtained from the Bureau of the Census, the Middle Tennessee Home Builders Association, Aladdin Resources, RCM interests, Baptist Hospital, Southeast Venture Companies, and various government agencies.

World's Fair spurred construction of hotels and motels as well as condominiums, apartments, and offices in anticipation of sustained increases in demand that did not occur. In Nashville, every category of construction was booming, and the first 10 months of 1983 were a peak period for housing starts. In the Memphis area the value of residential construction contracts rose 125 percent through November over the first 11 months of 1982. The value of nonresidential construction contracts increased by 10 percent.

Commercial construction improved as well. After staying below 5 percent in 1982, office vacancies in Nashville rose to over 13 percent by the second half of 1983 before falling to 11 percent by the third quarter. The surge was caused by increased supply and the consolidation of office space between two local insurance companies. Most of Memphis's large inventory of industrial space was absorbed. Despite the overall improvement in construction, employment continued to decline relative to year-earlier levels. At 72,000 in November, building-related employment was only 1,400 below the November 1982 level but 21,000 below peak 1979 levels.

The outlook for Tennessee construction is bright even though the rate of growth in home building may decelerate. The Nissan truck plant in Smyrna should generate substantial building nearby. Construction of more than six million square feet of office space in Nashville from 1983-1985, an increase of 50-80 percent over existing inventory, should buoy employment and demand for building materials. Major projects include a \$25 million renovation of office and retail space on Second Avenue, a \$25 million Washington Square complex, the \$50 million One Nashville Place office tower, a \$38-\$40 million office complex to house Northern Telecom's headquarters, and Baptist Hospital's continuing expansion. Despite this veritable explosion in office construction, industry analysts expect a high rate of absorption because of Nashville's diversified, service-based economy.

Chattanooga city officials are seeking \$4.6 million in Urban Development Action Grant funds for a \$28 million multi-use mall near the TVA's \$180 million Office of Power complex. This project would help integrate the revitalized areas of Chattanooga's central business district

by connecting the Chattanooga Choo-Choo hotel/entertainment complex with the TVA office center. Both projects should be complete by mid-1984. Major new construction projects in Memphis include a \$46 million, 406-room convention center hotel, the \$32 million One Memphis Place, and the \$42 million Morgan Keegan building.

Consumer Spending

Consumer spending patterns are determined largely by trends in personal income and population. Tennessee's total personal income growth has accelerated after sluggish performance during the recession years. For the 12-month period ending in mid-1983, personal income increased 6.3 percent, slightly higher than the nation's 6 percent gain. By the first half of 1983, Tennessee's personal income amounted to \$43.7 billion. Population growth, which slowed to .6 percent per annum in the April 1980-July 1982 period, should accelerate as recovery continues and migration rises. However, resumption of the growth rates of the 1970s is unlikely.¹⁸

Growth of retail sales in Tennessee trailed the increase in personal income, and employment in retail and wholesale trade declined slightly through the first eight months of 1983, but increased thereafter. Through August, taxable sales rose less than in 1982, when World's Fair visitors raised consumer spending to exceptionally high levels. However, the rate of growth accelerated in the third quarter of 1983. From July through November, total sales tax collections rose 13 percent. Building materials, auto dealers, and home furnishings registered the strongest increases of 30, 36, and 18 percent, respectively. Sales tax collections for the Tennessee SMSAs were up in all areas except Knoxville, where they declined 4 percent from the same period last year. Collections rose 9 percent in Chattanooga, 14 percent in Memphis, 16 percent in Nashville, and 6 percent in the Tri-Cities.¹⁹ By the Christmas shopping season, department store merchants in Nashville were registering double-digit increases in sales over

¹⁸U. S. Department of Commerce, Bureau of the Census, *Provisional Projection of the Population of States, by Age and Sex: 1980 to 2000*. Current Population Reports, Series P-25, No. 937, (August 1983), p. 11.

¹⁹*Monthly Statement of Revenue Collections*, Tennessee Department of Revenue, November 1983.

year-earlier levels, and most were optimistic about the holiday season. However, reports from retailers in the Tri-Cities indicated more modest performance and even some declines, in part because of a substantial decrease in the tobacco harvest.

Retail sales should continue to grow briskly in 1984. Faster employment, income, and population growth would further increase consumer spending. A \$60 million shopping mall, the second largest in Tennessee, should strengthen Nashville's status as a regional center for retail trade and could generate \$120 million in annual sales when completed in 1987. Construction may begin in the second half of 1984. Two new malls, each over 800,000 square feet, have opened near Memphis in the past two years. Wholesale traders in the locally important farm supplies market expect considerable improvement in 1984 because increased acreage should boost production substantially and continuing recovery should sustain demand. A \$50 million mall in Knoxville should boost that city's retail sector when it opens this summer.

Public Sector

The outlook for Tennessee's state and local government appears brighter than a year ago. By November, public sector jobs numbered 300,000, or 3,000 more than in November 1982 after declining since 1981. No other nonmanufacturing sector generated so many new jobs. Revenue collections exceeded estimates in the first four months of the fiscal year. Sales tax receipts in 1983 more than offset the shortfall in franchise and excise tax collections. The latter are Tennessee's counterpart to other states' corporate income taxes. Many corporations had filed for a six-month extension, from April to October, and receipts were less than expected.

Unlike prior years when hiring freezes and budget cutbacks were common, state government is likely to contribute to growth in 1984. The governor has proposed a \$5.1 billion budget for fiscal 1985, 14 percent higher than the 1984 budget. This increase would give state workers their first raise in 2 years and reward high-performance teachers through an incentive program. Financing would come from a 1 cent hike in the 4½ cent sales tax and other tax increases. Whether or not this budget wins

approval, continuing recovery should boost individual and corporate incomes, thereby fostering higher tax receipts, government hiring and spending.

However, the traditional stimulative role of the federal government in Tennessee's economy has diminished. Federal government employment declined 6 percent through the first three quarters. Defense expenditures for military functions in Tennessee (especially personnel costs) declined by 10 percent to \$1 billion in 1983; the Defense Department projects a mere 2 percent increase in 1984, the lowest of any southeastern state.²⁰ Federal civilian employment also is unlikely to rebound significantly. The TVA has been implementing cutbacks for several years, and more are likely in 1984.

Finance

Tennessee's commercial bank deposits were up 10 percent in November from the same month in 1982, an increase well below the 15 percent experienced by southeastern banks but slightly above the national increase. Savings placed in money market deposit accounts (MMDAs) paced this expansion by growing 127 percent. Federal Home Loan Bank Board figures indicate that bank time deposits declined by 9 percent. Savers were reluctant to place money in time deposits because market rates were rising and MMDAs offered a more liquid and attractive alternative.

Tennessee savings and loan associations posted double-digit deposit gains from March to November relative to year-earlier levels. By November, Tennessee thrifts had \$7.3 billion in deposits. MMDAs accounted for the majority of this growth. In response to the surge of home buying, Tennessee thrifts lent a healthy volume of mortgages in 1983. Commitments were up 70 percent from November to November. The 4 percent decline in mortgages outstanding since November 1982 reflects the trend of Tennessee S&Ls to discount in the secondary market a high proportion of the mortgages they made. Credit unions, outperforming both banks and S&Ls, registered a 14 percent deposit gain.

²⁰ U. S. Dept. of Defense, *Estimated Expenditures for States and Selected areas*, Fiscal Years 1983 and 1984.

Although depository institutions for the most part had a good year in 1983, a number of Tennessee banks failed in a crisis triggered by the February 14 collapse of the United American Bank of Knoxville. Bad loans, loss of loan participations with failed banks, and lack of confidence in some Tennessee banks caused the subsequent failures. Employment was virtually flat in Tennessee's financial sector. Slight declines occurred in the first eight months, but in November the number of jobs advanced slightly to 80,000. The performance of Tennessee's financial sector will be determined largely by developments in other state economic sectors.

A challenge facing the state's financial institutions is the growth of interstate banking. After focusing on the fast-growing Georgia and Florida markets, out-of-state banks, such as NCNB and Citicorp, have recently turned to Tennessee to offer consumer and housing loans and other financial services. Some Tennessee banks have begun to consolidate across county lines in response to state legislation enacted in 1983 to prepare them for interstate banking.

Tourism.

Travel accounted for \$3 billion of Tennessee's \$52 billion gross state product in 1981. In 1982 tourism generated 80,000 jobs, or 4.3 percent of total employment.²¹ The direct economic impact of Tennessee's tourism industry exceeds the \$1.8 billion generated by agriculture and roughly equals that of construction and finance in terms of jobs. Nashville had one-quarter of the state's travel-related employment, and middle Tennessee received 37 percent of travel expenditures. Memphis and mountainous east Tennessee are also important travel destinations. Memphis's Cook Convention Center, with 200,000 square feet of exhibit space, is the largest convention center in the state. West Tennessee received 27 percent of travel expenditures in 1981, and east Tennessee 36 percent.

Air travel statewide in 1983 was slightly above 1982 levels. However, Knoxville's plane passenger arrivals through November were off

11 percent. Chattanooga posted a 16 percent increase through November, and Nashville a 3 percent increase. Auto travel, as reflected in visitor center registrations, also declined. Through December, 2.1 million visitors registered at state welcome centers, 6 percent fewer than in the same period of 1982. Major private attractions had lower attendance than in 1982. Many of Tennessee's tourism indicators for 1983 were down because the World's Fair in Knoxville buoyed year-earlier figures to unusually high levels, new tourist attractions such as Disney's EPCOT Center in Florida offered intense competition, and the pace of recovery in Tennessee was slower than elsewhere. Less expensive attractions and those that rely more on local travel did show improvement in 1983. Tennessee National Park Service sites had 7 percent more visitors through October, and state parks registered a .2 percent increase through November.

Lodging tax receipts through November were down 15 percent from 1982 but up 9.9 percent over 1981 levels. Many Tennessee hotels and motels benefited from EPCOT-related travel along interstate corridors to Florida. However, Nashville's occupancy rate declined 3 percent to 67 percent, and Knoxville's plummeted 33 percent to 50 percent. Chattanooga's occupancy fell 5 percent to 62 percent through October. In contrast, Memphis's occupancy rate, 65 percent through October, was 2 percent better than in 1982.²²

Continuing recovery should lower unemployment and raise personal income, thereby fostering more discretionary spending for travel. Another important factor will be the 1984 New Orleans World's Fair. It should increase auto traffic, especially along Tennessee's interstate highways, boosting business at many hotels and motels. However, the World's Fair may command so much money and time that visitors will have little left for Tennessee attractions. As a hub between the Midwest and New Orleans, Memphis stands to gain the most traffic. Advance bookings for bus tours are very strong. The city is undergoing a revitalization that should boost its appeal to tourists. The historic Peabody

²¹Travel figures from **The Economic Impact of Travel on Tennessee Counties, 1982**, U.S. Travel Data Center (April 1983); gross state product estimates from **An Economic Report to the Governor of the**

State of Tennessee, Center for Business and Economic Research, University of Tennessee (January 1983), p. 95.

²²Pannell, Kerr, and Forster.

Hotel reopened in 1982 as a 450-room luxury hotel. Beale Street, the "birthplace of the blues," reopened in October after an \$11 million rebuilding program. The Mud Island attraction has drawn around 1 million visitors annually since it opened in 1981.

Refurbishing and promotion of the Natchez Trace Parkway should draw many fair visitors through middle Tennessee. The U. S. Department of the Interior has appropriated \$9.2 million for improving sections of the parkway in Tennessee. New or expanded attractions should also enhance the area's appeal to travelers. The Opryland theme park will open a \$3.7 million bobsled-type ride in June. Music Village USA, an ongoing entertainment complex, will add two country music museums this spring.

Nashville's convention business should improve with the \$50 million expansion of the 470-room Opryland Hotel, completed in 1983. A \$25 million convention center is under construction, but financial problems have stalled plans for a related hotel and renovation of Union Station into a retail complex. Of the major conventions already booked this year the American Society of Association Executives (ASAE) in March is widely regarded as the most important. One-fifth of the members of this organization, heads of 6,000 leading trade and professional associations, normally schedule subsequent meetings of their respective organizations in the host city. New and expanded carrier service implemented at year-end should boost Nashville's airport volume.

In east Tennessee, celebration of the 50th anniversary of the Great Smoky Mountains National Park should spur tourism. Scott County residents are awaiting the completion of a local national park site, the Southfork Recreation Area. This facility, begun four years ago, is opening in phases leading to completion in 1987-1988. The area's main attraction is a gorge with rapids for rafting. Also, hunting banned in nearby National Park Service facilities, will be open to the public. Knoxville and Chattanooga convention representatives are intensifying their marketing efforts. The renovated Knoxville Exhibition Hall will provide additional facilities to the area, but no new hotels are planned because of soft demand in 1983. Convention and city officials in Chattanooga are negotiating with a developer to construct a \$45 million hotel, parking garage,

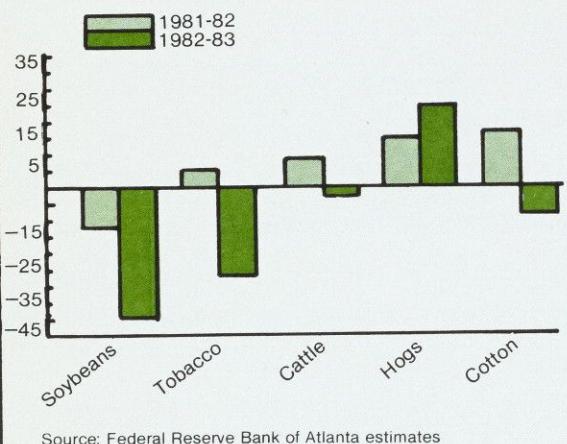
and trade center development to be completed by February 1985. White-water rafting should continue to boost Polk County's economy since the TVA agreed to refrain from diverting water from the Ocoee River throughout the tourist season.

Agriculture

The leading products for Tennessee's 92,000 farmers are soybeans, dairy and meat cattle, and tobacco. Together, these account for almost two-thirds of Tennessee's \$1.8 billion in farm cash receipts.²³ The dairy industry in middle and east Tennessee (see map) accounts for approximately 13 percent of Tennessee's farm revenue. The levy of milk assessments on production reduced the effect of price supports, and higher feed costs eroded profits in 1983. Many dairymen suffered losses severe enough to force liquidation. November's enactment of new dairy legislation, introducing financial incentives to reduce production, could improve the industry's prospects. Efficient producers are most likely to benefit, but high feed costs in the first half threaten to lower their profit margins. Marginal operations are likely to cease or cut back. Industry analysts believe milk production may have peaked in 1983.

Some 50,000 middle and east Tennesseans grow burley tobacco (see map) although most produce small volumes, averaging 1,300 pounds per farm, according to University of Tennessee Extension Service data. Tobacco production, of which 80 percent is burley, generates approximately 12 percent of the state's farm income. Tobacco is among the top three export commodities in Tennessee. Thus, the extreme damage to the drought-stricken tobacco crop in 1983 dealt a severe blow to Tennessee's economy. Over one-third of the 1983 crop was lost because of adverse weather; farmers had the worst yields in three decades. Much of the remaining tobacco was of an inferior quality and earned low prices, which were only slightly offset by the modest price supports granted to inferior tobacco. Preliminary estimates of income indicate a sharp decline (see Chart 3). The

²³ Economic Indicators of the Farm Sector, State and Income Balance Sheets Statistics, 1981, (October 1982) USDA Economic Research Service, pp. 121-122.

Chart 3. Percent Change in Farm Revenue

possibility of more favorable weather is the sole source of optimism for 1984. Tobacco growers face increasing pressure for major revisions in the tobacco program. High taxes and changing habits will continue to temper domestic consumption, and exports are unlikely to increase.

In west Tennessee, where production of soybeans, wheat, corn, cotton, pork, and cattle is concentrated (see map), farmers began 1983 in better financial condition than farmers in most other southern states. However, Tennessee experienced more severe crop damage than any southeastern state. Yields of soybeans, which contribute one-fifth of the state's farm cash receipts, fell 40 percent from a recent five-year average; cotton, 30 percent; and corn, 44 percent. The sharp drop in soybean yield was especially harmful since soybeans were

not included in the payment-in-kind (PIK) program. Crop incomes are expected to fall (see Chart 3). Livestock farmers suffered from declining prices. Crop shortages motivated cattle and pork farmers to rush their stock to market to avoid soaring feed costs. The resulting surfeit caused meat prices to fall. Nonetheless, some farmers may end the year with a profit (see Chart 3). Farmers enrolled in the PIK program will receive commodity payments, and those who increased crop insurance will receive additional assistance. Cattle prices should revive by mid-1984 as beef supplies grow tight.

Conclusion

Tennessee should see continued improvement in 1984. Employment gains in many industries have already served to lower the unemployment rate and should continue to do so in 1984. The rate of growth in residential construction may slow, but commercial construction should continue its healthy pace. Capital expansion plans for many of Tennessee's manufacturing operations will help maintain economic growth. However, nondurables manufacturing, especially chemicals, should improve modestly at best as foreign competition and export problems plague the industry. Personal income growth should stimulate consumer spending and tax revenues. Tennessee's financial community should continue to stabilize from 1983's problems and begin to consolidate for increased competition. Increased personal income and the World's Fair should stimulate tourism. The outlook for agriculture is more mixed; much will depend on foreign economies and the weather.

—**Bobbie H. McCrackin
and Paula Johannsen**