economic review

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IN THIS ISSUE

FEDERAL RESERVE BANK OF CLEVELAND

AN ECONOMIC PROFILE OF LEXINGTON, KENTUCKY

The Lexington, Kentucky, metropolitan area is on the road to industrial development and economic growth after being considered primarily as a tobacco and horse breeding center.[1]

There have been three distinct periods in the economic history of Lexington, with the development of natural resources dominating the first two periods. In the early 1800's, the area's economy was based mainly on the hemp industry, which supplied rigging for sailing vessels. Lowering of the import duties on hemp substitutes and development of steam-powered ocean vessels curtailed the hemp market about the time of the Civil War. Burley tobacco and Thoroughbred racehorses provided the foundation for the second period of economic development in Lexington. Although the City is still the largest loose-leaf tobacco market in the nation, as well as the center of the racehorse industry, Lexington recently entered an industrial phase—the third period of development—which is the focus of this article.

POPULATION GROWTH

Population in the Lexington SMSA has increased substantially and steadily over the longer run as well as in recent years. During the period 1900-64, the number of inhabitants in Fayette County more than tripled, increasing from 42,000 to 148,400; in comparison, for example, population in Kentucky as a whole increased by only 47 percent (see Table I). While Louisville and Cincinnati (located on the Ohio River) both outdistanced Lexington in the "steamboat era" beginning in the 1820's, both have experienced slower rates of population increase than Lexington since 1900.

The rate of population growth in the Lexington area has increased in each decade since 1900 with the exception of the depression decade of the 1930's. Even in that period, however, Lexington recorded a substantially

TABLE I

Percent Increases in Population, 1900-64

Lexington SMSA Compared with Selected Areas

	Lexington	Louisville	Cincinnati	Kentucky	Ohio
1900-64	253%	162%	149%	47%	144%
1900-10	13	10	12	7	15
1910-20	14	7	7	6	21
1920-30	25	22	20	8	15
1930-40	15	7	4	9	4
1940-50	28	28	15	3	15
1950-60	31	26	19	3	22
1960-64	13	6	4	4	4

NOTE: The Lexington SMSA had an estimated population of 148,400 in 1964 compared with 770,000 for the Louisville SMSA and 1,313,000 for the Cincinnati SMSA.

Sources: U. S. Department of Commerce; Kentucky Department of Commerce; Lexington-Fayette County Chamber of Commerce

[1] The Lexington SMSA is coterminous with Fayette County, Kentucky.

larger population increase than the selected areas shown in Table I. The rapid population gains of Lexington have in part reflected migration from surrounding areas encouraged by increasing job opportunities in the metropolitan area.

NONAGRICULTURAL EMPLOYMENT

From 1960 to 1965, nonagricultural employment in the Lexington SMSA increased by nearly 41 percent compared with 12 percent for Louisville and 16 percent for Kentucky as a whole (see Table II). Consequently, Lexington's share of total nonagricultural employment in Kentucky increased from 6.7 percent to 8.1 percent. Manufacturing employment in Lexington increased 36 percent in the 1960-65 period while nonmanufacturing employment recorded a 42 percent gain; in both categories, the percentage gains were considerably higher than those for either Louisville or Kentucky. In 1965, nonmanufacturing employment accounted for nearly 80 percent of total nonagricultural employment in the Lexington area.

NONMANUFACTURING EMPLOYMENT

Government, wholesale and retail trade, and services are the main sources of nonmanufacturing employment in the Lexington SMSA. In 1965, these three sources accounted for about 79 percent of nonmanufacturing employment and for almost two-thirds of total nonagricultural employment in Lexington; the latter proportion compared with about one-half of total nonagricultural employment in the State and in Louisville.

Government is the largest single source of employment in Lexington. In 1965, 17,300 persons, or 28 percent of all nonagricultural workers in Lexington, were employed by Federal, state, or local government. The proportion of government employment in Lexington in 1965 was above that of Kentucky, Ohio, the U. S., and the selected SMSA's shown in Table III. Government has been a growth "industry" in Lexington, with employment of this type increasing by 80 percent during 1960-65, and from 22 percent of total nonfarm employment in 1960 to 28 percent in 1965. The relatively high proportion of government workers in Lexington reflects a large number of special government enterprises located in the City in addition to the normal complement of State and local government services typically found in a metropolitan area. For example, with nearly 50 elementary, junior and senior high schools, and with the University of Kentucky located in Lexington, employment in public education accounts for half of total government employment in the area. In addition, employment associated with public health services contributes to the large number employed in government in Lexington, with two Federal hospitals—for drug addiction and psychiatric care of veterans—as well as a state mental hospital located there. Federal Government employment is augmented by a military establishment. Finally, since Lexington is the county seat for Fayette County, local government administration offices are located in the City.

The importance of trade and service employment in Lexington—the third and fourth largest sources of nonagricultural employment—reflects the central city's status as the trade and service center for surrounding

TABLE II

Nonagricultural Employment by Major Category, Annual Averages, 1960 and 1965

Lexington SMSA Compared with Selected Areas

	Number Employed (thousands)						Percent Change 1960-65			Percent of Kentucky Total			
	Lexington		Louisville		Kentucky		Lexington	Louisville	Kentucky	Lexington		Louisville	
	1960	1965	1960	1965	1960	1965				1960	1965	1960	1965
Total Nonagricultural Employment	43.8	61.6	242.1	270.6	653.6	758.1	+40.6%	+11.8%	+16.0%	6.7%	8.1%	37.0%	35.7%
Manufacturing—Total	9.7	13.2	84.8	94.5	171.6	206.1	+36.0	+11.4	+20.1	5.7	6.4	49.4	45.8
Food and Kindred Products	1.2	1.2	13.8	12.1	26.1	25.1	-0-	—12.3	— 3.8	4.5	4.9	52.9	48.2
Tobacco	1.5	1.2	8.3	8.8	11.3	12.5	—20.0	+ 6.0	+10.6	13.7	9.5	73.5	70.4
Textiles and Apparel	0.5	0.8	2.5	2.5	23.1	28.1	+60.0	-0-	+21.6	2.1	3.0	10.8	8.9
Printing and Publishing	0.6	0.8	5.9	6.1	8.1	9.8	+33.3	+ 3.4	+21.0	7.6	8.0	72.8	62.2
Metal and Machinery*	5.0	7.5	30.4	37.3	61.2	80.8	+50.0	+22.7	+32.0	8.2	9.3	49.7	46.2
Other Manufacturing	0.9	1.7	23.9	27.7	41.8	49.9	+82.0	+15.9	+19.4	2.1	3.2	57.2	55.5
Nonmanufacturing—Total	34.1	48.4	157.3	176.1	482.0	551.9	+41.9	+12.0	+14.5	7.1	8.8	32.6	31.9
Construction	2.9	4.6	12.7	13.9	35.9	47.3	+58.6	+ 9.4	+31.8	8.0	9.7	35.4	29.4
Transportation and Public Utilities	2.3	2.9	21.2	20.9	52.5	54.0	+26.1	— 1.4	+ 2.9	4.4	5.4	40.4	38.7
Trade	10.5	12.4	52.3	58.2	139.8	155.3	+18.1	+11.3	+11.1	7.5	8.0	37.4	37.5
Finance	1.4	2.6	12.1	14.0	25.0	29.8	+85.7	+15.7	+19.2	5.7	8.8	48.4	47.0
Services	7.3	8.5	32.2	39.1	84.8	101.9	+16.4	+21.4	+20.1	8.7	8.4	38.0	38.4
Government	9.6	17.3	26.8	30.0	110.1	135.5	+80.2	+11.9	+23.1	8.7	12.8	24.3	22.1
Education	n.a.	9.6	n.a.	n.a.	41.8	55.8	n.a.	n.a.	+33.5	n.a.	17.2	n.a.	n.a.

* Includes SIC codes 33, 34, 35, 36, and 37.

n.a. Not available.

Sources: Kentucky Department of Economic Security and U. S. Department of Labor

TABLE III

Distribution of Nonagricultural Employment

Seven Major Employment Categories, Annual Average, 1965

Lexington SMSA Compared with Selected Areas

Percent in Government		Percent in Manufacturing		Percent in Trade		Percent in Services	
Lexington	28.1%	Ohio	39.2%	Louisville	21.6%	Columbus	14.9%
Columbus	20.6	Cincinnati	35.3	Cincinnati	20.9	U. S.	14.7
Kentucky	17.9	Louisville	34.9	Columbus	20.9	Louisville	14.4
U. S.	16.6	U. S.	29.8	U. S.	20.8	Lexington	13.9
Ohio	13.7	Kentucky	27.2	Kentucky	20.5	Cincinnati	13.6
Cincinnati	12.8	Columbus	26.1	Lexington	20.1	Kentucky	13.4
Louisville	11.1	Lexington	21.4	Ohio	19.4	Ohio	12.7

Percent in Construction		Percent in Transportation, Communication, and Public Utilities		Percent in Finance	
Lexington	7.4%	Louisville	7.7%	Columbus	6.2%
Kentucky	7.1	Cincinnati	7.6	Cincinnati	5.4
U. S.	5.3	Kentucky	7.1	Louisville	5.2
Louisville	5.1	U. S.	6.7	U. S.	5.0
Columbus	4.9	Columbus	6.1	Lexington	4.2
Cincinnati	4.3	Ohio	6.0	Ohio	3.9
Ohio	4.3	Lexington	4.8	Kentucky	3.9

Sources: U. S. Department of Labor; Division of Research and Statistics, Ohio Bureau of Unemployment Compensation; Kentucky Department of Economic Security

counties as well as Fayette County. Nevertheless, the 16 percent increase in service employment in Lexington during 1960-65 was somewhat less than that recorded by either Louisville or Kentucky (see Table II). In contrast, employment in wholesale and retail trade in Lexington increased 18 percent from 1960 to 1965 compared with 11 percent for both Louisville and the State as a whole. It appears likely that Lexington will become an even more important distribution center, particularly for eastern Kentucky, as the interstate highway system nears completion and extends the City's market area. Completion of the interstate highways will also increase the industrial attraction of Lexington as I-75 and connecting routes will provide quick access to major southern markets such as Atlanta, New Orleans, and Memphis as well as to midwestern centers including Cin-

cinnati, Cleveland, and Chicago while I-64 will reduce the transportation time to Louisville.

Employment in construction is also relatively important in the Lexington SMSA, increasing sharply from 1960 to 1965 (see Table II). As a result, the area's share of the State total increased from 8.0 percent in 1960 to 9.7 percent in 1965. Interestingly, the proportion of workers employed in construction in Lexington is greater than in the U. S., Kentucky, Ohio, or any of the selected SMSA's shown in Table III. While nonresidential construction in Lexington posted significant gains between 1961 and 1965 (the only period for which data on construction in Lexington are available), residential building did even better, nearly tripling in dollar value (see Table IV). In comparison, during 1961-65 residential construction in Kentucky as a whole was up 83 percent, and in the U. S., was up 32 percent.

MANUFACTURING EMPLOYMENT

Manufacturing is the second largest source of nonagricultural employment in Lexington although the proportion of total employment in this category is substantially smaller than that in the selected areas shown in Table III. While the number employed in manufacturing increased by 36 percent during 1960-65, manufacturing employment as a percent of total nonagricultural employment in Lexington declined fractionally (from 22.0 percent to 21.4 percent); the 36 percent increase in Lexington during 1960-65 compared with 20 percent in Kentucky and only 11 percent in Louisville. During the same period, the proportion of manufacturing employment in Kentucky accounted for by Lexington increased from 5.7 percent to 6.4 percent of the total.

The production of machinery provides the most important source of manufacturing employment in the Lexington SMSA, and in 1965

TABLE IV

Building Contracts, 1961-65

Lexington SMSA Compared with Selected Areas

	Millions of Dollars					Percent Change
	1961	1962	1963	1964	1965	1961-65
Total						
Lexington SMSA	$ 31.5	$ 49.2	$ 47.2	$ 63.7	$ 78 9	+150.5%
Kentucky	293.7	347.5	394.7	445.8	514.0	+ 75.0
U. S.	28,238.5	31,048.8	34,879.4	36,086.5	38,466.7	+ 36.2
Residential						
Lexington SMSA	20.7	26.5	34.3	46.6	58.0	+180.2
Kentucky	182.1	190.7	256.7	283.8	332.6	+ 82.6
U. S.	16,123.4	18,038.6	20,502.0	20,564.6	21,247.5	+ 31.8
Nonresidential						
Lexington SMSA	10.8	22.7	12.9	17.1	20.9	+ 93.5
Kentucky	111.6	156.8	138.0	162.0	181.4	+ 62.5
U. S.	12,115.1	13,010.2	14,377.4	15,521.9	17,219.2	+ 42.1

Source: F. W. Dodge Company

(along with a small amount of metal manufacturing) accounted for 7,500 jobs, more than one-half of all manufacturing employment in Fayette County (see Table II). Two companies (one manufactures typewriters and the other, switchgears and switchboards) account for nearly three-fourths of all persons employed in these categories. These two large manufacturing plants are branches of major corporations headquartered in other states as is also true of other large employers in Lexington. The situation is indicative of the fact that the area's manufacturing base is geared largely to reliance on "outside capital" and is concentrated in relatively few companies.

Tobacco processing, although highly seasonal, is another important source of manufacturing employment in Lexington, which would be expected in view of the large volume of tobacco raised in the area. (As is seen later, much of the nation's burley tobacco crop is grown in Fayette and surrounding counties.) In 1965, employment in tobacco manufacturing averaged 1,200, but ranged, on a monthly basis, from a low of 300 to a high of 2,600. From 1960 to 1965, employment in tobacco processing declined 20 percent due largely to changes in technology. Previously, burley tobacco was stemmed and redryed in Lexington immediately after being sold at auction in the fall. The tobacco was then packed and stored for aging in a warehouse, either in Lexington or elsewhere. Now, however, the tobacco is packed in hogsheads immediately after the auction sales and shipped directly to processing plants in other parts of Kentucky or North Carolina where it is redryed and threshed.

MEASURES OF MANUFACTURING ACTIVITY

Table V shows year-to-year changes in three major measures of manufacturing activity—employment, value added, and capital spending. Manufacturing employment in Lexington increased in every year from 1958 to 1963, outpacing the State and the U. S. both in each year and for the period as a whole. Gains in value added by manufacture in Lexington also generally outperformed both the U. S. and Kentucky from 1958 to 1963.

Fluctuations in capital spending in Lexington were greater than that for either the U. S. or Kentucky from 1958 to 1963, as can be seen in Table V. This is a normal situation when data covering a relatively small area are used. Nevertheless, the $51.1 million of capital spending in Lexington during 1958-63 was substantial and represented 6.4 percent of the total spent in the State over the five-year period. Moreover, if 1959 were the base rather than 1958, the showing of Lexington would be much more favorable; for example, during 1959-63, capital spending in Lexington increased 78 percent compared with 118 percent in Kentucky and 30 percent in the U. S.

Electric power consumption by manufacturers, which may be used as a proxy for regional industrial production, increased at an average annual rate of 9.6 percent in Lexington between 1958 and 1965, compared with 6.9 percent in the Louisville SMSA. As shown in Table VI, in 1965 the electric power index for Lexington stood at

TABLE V

Measures of Manufacturing Activity, 1958-63

Lexington SMSA Compared with Selected Areas

Percent Change From Previous Year	Employment			Value Added			Capital Spending		
	Lexington	Kentucky	U. S.	Lexington	Kentucky	U. S.	Lexington	Kentucky	U. S.
1959	+14.7%	+7.1%	+4.1%	+41.4%	+16.6%	+14.0%	—62.9%	— 5.7%	— 8.3%
1960	+ 3.6	—0.7	+0.6	+ 1.1	— 5.6	+ 1.7	+19.0	+ 4.0	+14.4
1961	+ 5.8	—2.1	—2.7	+ 6.1	+ 4.0	+ 0.1	—17.5	+14.4	— 3.0
1962	+ 4.4	+3.9	+2.8	+21.9	+ 9.0	+ 9.2	+83.2	+15.0	+ 6.8
1963	+ 6.6	+2.7	+4.9	+11.4	+15.5	+ 6.0	— 1.5	+61.3	+ 9.3
Percent Change 1958-63*	+40.0	+11.2	+10.0	+105.9	+44.1	+34.3	—34.1	+105.4	+18.8

* Data for the Lexington SMSA are available only from 1958 to 1963.

Source: U. S. Department of Commerce

175 compared with 152 for Louisville and 138 for the Fourth District as a whole.

FINANCIAL PATTERNS

Selected financial series also suggest a strong growth pattern for Lexington. For example, bank debits, which measure check-writing activity and are an indicator of economic activity in a local area, more than doubled in Lexington from 1958 to 1965, compared with increases of 81 percent and 74 percent, respectively, in the U. S. and the Fourth District (and 69 percent in Louisville). (See Table VII.) Similarly, total loans at insured commercial banks in Lexington increased 120 percent from 1958 to 1965 while those for all insured banks in Kentucky moved up 98 percent. Lexington banks increased their share of commercial bank loans in Kentucky from 7.2 percent to 8.1 percent (see table below). Demand deposits at banks in Lexington also increased as a proportion of the total in the State, or from 5.5 percent in 1958 to 6.3 percent in 1965, while time deposits increased from 7.2 percent to 7.7 percent.

Loans and Deposits at Lexington Banks as Percent of State Totals

	1958	1965
Total Loans	7.2%	8.1%
Demand Deposits	5.5	6.3
Time Deposits	7.2	7.7

Sources: Federal Deposit Insurance Corporation and Federal Reserve Bank of Cleveland

ECONOMIC FLUCTUATIONS

The economic climate of Lexington seems to have been less affected by the business cycle than that of either Kentucky or the U. S. in recent years. This is at least suggested by the behavior of series on employment, electric power consumption, and the rate of unemployment. In part, the relative immunity to the business cycle reflects the high proportion of stable economic activities in the area, including government, trade, and services, as well as the smaller proportion of manufacturing activity as compared with other areas. The relative stability of economic activity in Lexington is implied in the fact that neither employment nor industrial consumption of electric power showed a decline in any year during 1958-65, which was not

TABLE VI

Selected Indicators of Industrial Activity

Lexington SMSA Compared with Selected Areas

Manufacturing Employment	1958	1959	1960	1961	1962	1963	1964	1965	Percent Change 1958-65
Lexington	7,798	8,948	9,269	9,806	10,240	10,916	12,446†	13,200†	+ 69.2%
Kentucky	162,243	173,843	172,714	169,123	175,784	180,460	192,200†	206,200†	+ 27.1
U. S. (thousands of persons)	15,422	16,059	16,159	15,728	16,163	16,962	17,259†	18,032†	+ 16.9
Value Added by Manufacture									**1958-63**
Lexington (thousands of dollars)	$ 77,342	$109,345	$110,576	$117,341	$143,000	$159,287	n.a.	n.a.	+105.9
Kentucky (millions of dollars)	1,769	2,063	1,947	2,025	2,207	2,549	n.a.	n.a.	+ 44.1
U. S. (millions of dollars)	141,500	161,315	164,003	164,179	179,290	189,995	n.a.	n.a.	+ 34.3
Manufacturing Activity									**1958-65**
Lexington (Index 1958-59=100)*	91.9	108.1	112.7	122.1	136.3	144.2	164.0	174.6	+ 90.0
Louisville (Index 1957-59=100)*	94.8	107.6	100.8	103.6	114.6	125.8	139.0	151.6	+ 59.9
Fourth District (Index 1957-59=100)*	92.7	104.9	106.7	103.8	111.0	117.7	127.6	138.4	+ 49.3
U. S. Index of Industrial Production (Manufacturing Component)	100.2	109.9	103.0	109.6	118.7	124.9	133.1	145.0	+ 44.7

* Manufacturing activity based on electric power consumption by manufacturers.

† Figures may not be comparable to preceding years because of difference in source.

n.a. Not available.

Sources: U. S. Department of Commerce; U. S. Department of Labor; Board of Governors of the Federal Reserve System; Federal Reserve Bank of St. Louis; Federal Reserve Bank of Cleveland

TABLE VII

Selected Indicators of Financial Activity, 1958-65

Lexington SMSA Compared with Selected Areas

	1958	1959	1960	1961	1962	1963	1964	1965	Percent Change 1958-65
Bank Debits (millions of dollars, annual average)									
Lexington (center only)	$ 127.9	$ 149.2	$ 159.5	$ 165.6	$ 190.7	$ 212.4	$ 238.6	$ 260.0	+103%
Louisville (center only)	883.5	945.6	935.4	961.2	1,005.0	1,142.6	1,266.2	1,489.0	+ 69
35 Fourth District Centers	13,082.0	14,583.6	15,330.7	15,604.2	17,077.1	18,612.4	20,724.0	22,694.0	+ 74
U. S. (excluding New York City)	123,419.0	137,963.0	144,659.0	152,691.0	168,380.0	183,224.0	200,405.0	222,810.0	+ 81
Selected Series at Insured Commercial Banks (millions of dollars, yearend)									
Total Loans									
Lexington	$ 65.0	$ 74.4	$ 80.3	$ 79.7	$ 93.5	$ 106.4	$ 125.1	$ 143.0	+120%
Kentucky	898.8	999.5	1,079.7	1,134.9	1,248.4	1,413.5	1,575.0	1,775.2	+ 98
U. S.	98,131.7	110,694.9	117,521.6	124,807.4	140,023.3	155,933.4	175,096.2	201,114.1	+105
Demand Deposits									
Lexington	97.2	102.9	96.4	114.7	119.9	135.1	141.8	146.6	+ 51
Kentucky	1,778.5	1,805.2	1,771.5	2,044.0	2,056.3	2,029.2	2,257.7	2,321.8	+ 31
U. S.	149,488.0	151,538.2	155,709.3	165,092.9	163,216.6	162,952.1	178,691.2	183,836.9	+ 23
Time Deposits									
Lexington	33.0	35.5	35.9	37.8	50.4	60.5	72.0	85.7	+160
Kentucky	454.8	488.3	519.8	572.2	697.4	795.9	936.0	1,118.3	+146
U. S.	65,680.7	67,473.3	73,283.9	82,811.9	98,227.0	111,694.5	127,539.0	147,675.8	+125

Sources: Federal Deposit Insurance Corporation and Federal Reserve Bank of Cleveland

the case for the selected areas included in Table VI.

The behavior of the rate of unemployment also provides evidence of the moderating influence of the economic mix in Lexington. For example, the unemployment rate for workers covered by unemployment compensation in Lexington was at a lower level during the 1960-61 recession than the rate in Kentucky, the U. S., or any of the selected areas shown in Table VIII except Columbus. Moreover, as Table VIII shows, the decrease in unemployment in Lexington since 1961 compares favorably with the showings of other relatively low unemployment areas, for example, Columbus.

TABLE VIII

Unemployment Rates For Workers Covered by Unemployment Compensation

Lexington SMSA Compared with Selected Areas

Annual Averages, 1960-65

	1960	1961	1962	1963	1964	1965
Lexington	3.7%	4.3%	3.1%	2.3%	2.0%	1.4%
Louisville	5.0	5.3	3.3	2.9	2.4	1.7
Kentucky	7.0	7.9	5.7	4.8	4.4	3.2
U. S.	4.8	5.6	4.4	4.3	3.7	3.1
Ohio	4.7	5.7	4.1	3.7	2.7	1.9
Cincinnati	3.9	4.8	2.9	2.7	3.0	2.2
Columbus	3.2	3.6	2.1	2.1	2.0	1.3

Sources: U. S. Department of Labor; Kentucky Department of Economic Security; Bureau of Research and Statistics, Ohio Department of Unemployment Compensation

BLUEGRASS AGRICULTURE

An economic profile of Lexington would not be complete without mention of the area's agriculture, especially burley tobacco and Thoroughbred racehorses.[2] Lexington is situated in the center of Kentucky's fertile "inner bluegrass area" where agricultural land value is extremely high, due partly to burley tobacco allotments that determine the number of acres of tobacco each farm can grow under the Federal Government's price support program.[3] Kentucky produces annually two-thirds of the nation's burley tobacco crop, which is used mainly in cigarette production, and Fayette County is the largest producer in the State.[4] Lexington's position as the largest loose-leaf tobacco market in the nation reflects the City's location in the center of the State's tobacco growing area. Auction sales of burley tobacco, which begin each year in mid-November and continue until early February, usually gross more than $55 million.

Lexington has also long been recognized as the center of the Thoroughbred racehorse industry.[5] Originally, the bluegrass area around Lexington developed as a horse-raising region because of local advantages, especially soil, which, with a high level of

[2] Agricultural employment in the Lexington SMSA amounted to 1,526 in 1959, and in that year accounted for 3.4 percent of total employment in the area.

[3] In 1959, the average value of land and buildings in Fayette County was $104,638 per farm and $484 per acre compared with an average of $14,300 per farm and $133 per acre for the State as a whole. In Ohio, which has a higher proportion of fertile, tillable land (47 percent compared with 39 percent for Kentucky), the 1959 per acre value averaged $245 and the average farm was valued at $32,697.

[4] See "A Look at Burley Tobacco," *Monthly Business Review*, Federal Reserve Bank of Cleveland, Cleveland, Ohio, October 1963.

[5] See "Thoroughbreds in Kentucky," *Economic Review*, Federal Reserve Bank of Cleveland, Cleveland, Ohio, April 1964.

phosphate and calcium, promotes strong bone structure. Concentration of racehorse breeding farms in the Lexington area encouraged the establishment of many related businesses including clinics for the advanced medical treatment of horses, specialized food, transportation, and insurance services, the printing and publishing of trade magazines, blacksmithing, and the world-famous horse auctions. Six separate sales of Thoroughbred racehorses are held during the year at the Keeneland racetrack and in 1965, 2,700 horses were sold at these sales for $16 million.

There is some concern in Lexington that the Thoroughbred industry is moving out of the region. What seems to be happening, however, is not that the industry is leaving the area, but that it is growing more rapidly in other places, and becoming more geographically diversified. Thus, even though the proportion of the total foal crop born in Kentucky has declined substantially in recent years, the number born there has actually increased, as shown by the following:

Thoroughbred Foal Registrations
Selected States and Canada
Number Born and Percent of Total Crop

	1957		1964	
	Number	Percent	Number	Percent
Kentucky	3,061	29%	3,255	19%
California	1,502	14	2,668	16
Canada	803	8	1,211	7
Florida	237	2	882	5
Maryland	485	5	877	5
Virginia	625	6	831	5
Illinois	267	3	763	5

Source: *The Blood-Horse*, March 12, 1966

CONCLUDING COMMENTS

The image usually associated with Lexington seems to be yielding to one of greater economic diversification and industrial growth. Most available measures of economic activity in Lexington, including employment, value added by manufacture, electric power consumption, bank debits, loans, and deposits, have exhibited large gains in recent years. Because many of these indicators are available only for recent years, however, it is difficult to determine whether the area is experiencing a "catching-up phase" in industrial development following an extended period as an agriculturally-oriented economy, or whether a new set of economic forces is changing the basic orientation of the area.

With the latter appearing to be the case, Lexington's well-known social and cultural environment, the locational advantages of a completed interstate highway system, and continued expansion of educational facilities represent strong inducements for substantial industrial growth in the period ahead. Thus far, Lexington has been relatively immune to the vagaries of the business cycle. It will be interesting to see if this record can be maintained in the face of industrial expansion. The task would, of course, be lightened by a perpetuation of at least a semblance of the economic mix that has prevailed up to now.

RECENT PATTERNS IN TERM LENDING

Through the first half of 1966, term loans by banks to business firms had been expanding more rapidly than total business loans, but with less attendant publicity.[1] The escalation in term lending to business started around midyear 1964, and continued until the second half of 1966, when such lending slackened along with more moderate increases in total business loans.

BACKGROUND

As indicated in Chart 1, commercial and industrial loans at weekly reporting banks in the U. S. have increased throughout the economic expansion that began in 1961. But, as the chart also shows, the pace of such loans picked up appreciably beginning in mid-1964. A similar pattern is evident for reporting banks in New York and in the Fourth Federal Reserve District (see Chart 1). The relevant figures on commercial and industrial loans at weekly reporting banks are as follows (at an annual rate):

	Fourth Quarter 1961 to Second Quarter 1964	Second Quarter 1964 to Second Quarter 1966
U. S.	7%	22%
New York	4	28
Fourth District	8	27

While figures on term loans are not available for all weekly reporting banks in the U. S., such information does exist for banks in New York and in the Fourth District, as well as for bank term loans to manufacturing firms, as reported by the Federal Trade Commission and the Securities and Exchange Commission. For the same periods discussed above, the relevant figures on increases in term loans are as follows (at an annual rate):

	Fourth Quarter 1961 to Second Quarter 1964	Second Quarter 1964 to Second Quarter 1966
FTC-SEC Series	5%	46%
New York	6	32
Fourth District	10	32

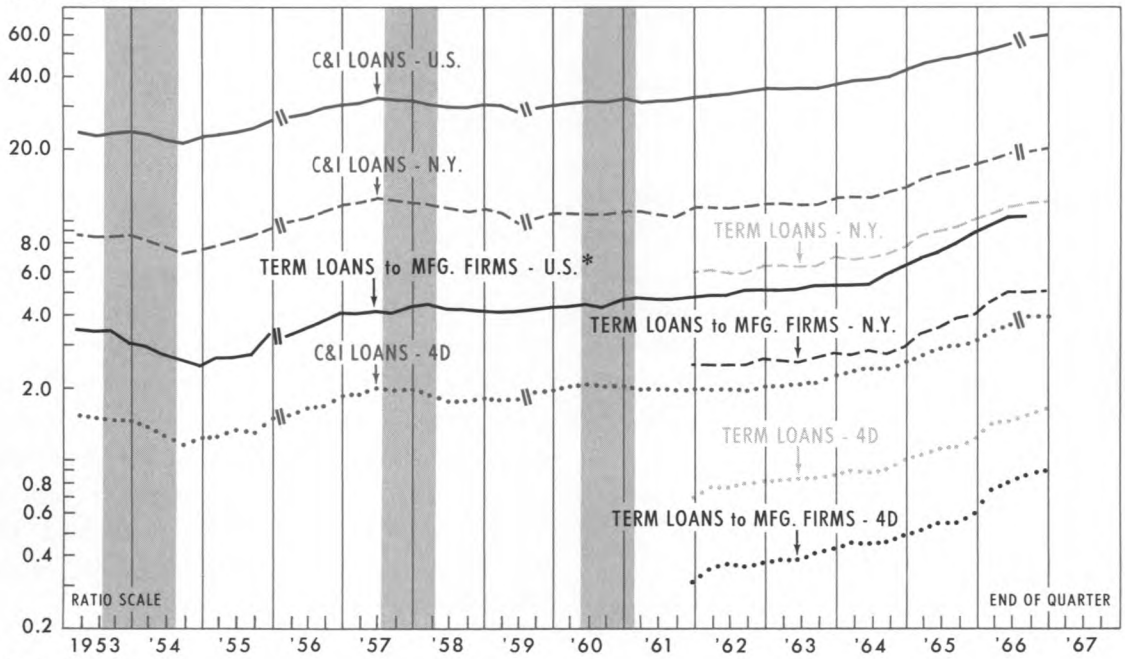
The sharp increase in the volume of term lending beginning in mid-1964 raises questions as to why the surge in term lending occurred, as well as to the possible implications. For example, are there specific factors that accounted for the acceleration in term lending? Was the surge in term lending typical or significant? How long can a rapid expansion of term lending be sustained? Was

[1] A term loan usually has an original maturity of more than one but less than ten years. Term loan data include revolving credit agreements, which are short-term notes that may be renewed for a longer term—often up to two years—in accordance with formally stated arrangements, but do not include informal lines of credit.

Chart 1.

SELECTED SERIES on COMMERCIAL and INDUSTRIAL LOANS and TERM LOANS

Billions of dollars



‖ Break in Series

* FTC-SEC Series. All other data are from weekly reporting banks.

Sources of data: FTC-SEC; Federal Reserve Bank of New York; Federal Reserve Bank of Cleveland

the recent spurt primarily cyclical, or was there a change in long-term trend? What factors influence the supply of and demand for term loans? Some of these questions may already be answered by the slackening in the pace of term lending in recent months. Nevertheless, the sharp break with previous patterns appears to make it worthwhile to examine some of the factors underlying the behavior of term lending.

Unfortunately, analysis in this area runs into the problem of insufficient availability of data.[2] The only time series on term loans that are presently available include: (1) The Federal Trade Commission—Securities and Exchange Commission's series in the *Quarterly Financial Report for Manufacturing Corporations* under "Long-term debt due in more than one year, (a) Loans from banks"; (2) the weekly series available from the Federal

[2] This problem will be partly solved by the collection of term lending information at weekly reporting banks throughout the U. S. which began in January, although it will be some time before sufficient time series data are available.

Reserve Bank of New York on term loans made by a sample of weekly reporting banks in New York City; and (3) a similiar series at the Federal Reserve Bank of Cleveland for weekly reporting banks in the Fourth District.[3]

All three of these series highlight the acceleration in term lending beginning in mid-1964 alluded to earlier. As shown in Table I, the FTC-SEC series posted a 19.8 percent gain during all of 1964, but that gain included a 17.9 percent increase in the second half of the year. In 1965, term loans in the FTC-SEC series registered a gain of 39.7 percent, with the pace essentially maintained in the first half of 1966. At New York banks, the pattern was similar, with term loans posting substantial gains beginning in the second half of 1964. The rise in the Cleveland series was somewhat less abrupt as sizable gains had been posted steadily since the inception of the series. As indicated earlier, the percentage gains of term loans in the two Reserve bank series outstripped the increases in total commercial and industrial loans beginning in mid-1964.

Term borrowing from commercial banks also increased more rapidly than other longer term financing by manufacturing corporations in the period under review, so that term loans accounted for a larger proportion of the total long-term debt of manufacturing concerns. The shift in the share of long-term debt of manufacturing corporations accounted for by term loans, at selected intervals, is as follows:

Yearend 1960	14.8%
Yearend 1963	13.9
End of Second Quarter 1964	14.0
Yearend 1964	15.6
Yearend 1965	18.9
End of Second Quarter 1966	19.8
End of Third Quarter 1966	19.2

The change in relationships is supported by the figures shown in Table II. Beginning in the second half of 1964, term loans to manufacturing firms grew considerably faster than did long-term debt, a pattern that continued through the first half of 1966. (Other long-term debt includes chiefly bonds, notes, debentures, and certain mortgages.)

SUPPLY-DEMAND RELATIONSHIPS FOR TERM LOANS

The acceleration in term lending beginning at mid-1964 surprised some observers

[3] None of these series is sufficiently comprehensive to allow complete and detailed analysis. While the two Federal Reserve series cover all commercial and industrial borrowers at reporting banks, the New York series dates back only to 1960, and the Cleveland series only to 1961. The FTC-SEC series covers debt owed to banks by manufacturing corporations only, and there is evidence that manufacturing firms do not account for the majority of term loans outstanding at banks. For example, in the Fourth District, where term loan statistics are available by industry for nonmanufacturing as well as manufacturing firms, the ratio of term loans to manufacturing firms to total classified term loans (commercial and industrial) on a quarterly basis averaged 48.7 percent from the fourth quarter 1961 through the third quarter 1966. A similar computation for the New York series indicates that the corresponding average is only 40.1 percent. Nevertheless, the fact that, over time, term borrowing by nonmanufacturing firms does not vary widely in the case of either trend or cyclical behavior allows some generalizations to be made. (Although the proportion of term loans accounted for by manufacturing firms rose in 1966, the ratio of term loans to manufacturing corporations to total term loans deviated from the mean value of the time period under consideration by about plus or minus 8 percent in the Cleveland series, and only by about plus or minus 2½ percent in the New York series.)

TABLE I

Percent Changes in Term Loans

		New York City		Fourth District	
	Term Loans to Manufacturing Firms (FTC-SEC Series)	Total Term Loans	Term Loans to Manufacturing Firms	Total Term Loans	Term Loans to Manufacturing Firms
1962	+ 7.6%	+ 6.8%	+ 4.6%	+13.9%	+15.2%
1963	+ 3.1	+ 9.9	+ 5.7	+ 6.8	+12.9
1964	+19.8	+ 9.9	+ 6.2	+16.3	+16.5
1965	+39.7	+29.3	+37.9	+22.8	+20.4
1966	n.a.	+18.2	+27.5	+33.0	+53.8
1st. half 1964	+ 1.7	— 1.0	+ 1.6	+ 3.7	+ 6.2
2nd. half 1964	+17.9	+11.0	+ 4.5	+12.2	+ 9.7
1st. half 1965	+14.4	+15.3	+21.8	+11.4	+10.6
2nd. half 1965	+22.1	+12.2	+13.2	+10.2	+ 8.9
1st. half 1966	+16.6	+13.8	+23.0	+18.5	+35.6
2nd. half 1966	n.a.	+ 4.2	+ 3.6	+12.2	+13.4
1st. quarter 1966	+ 7.1	+ 7.8	+13.1	+13.9	+27.1
2nd. quarter 1966	+ 8.9	+ 5.5	+ 8.8	+ 4.1	+ 6.7
3rd. quarter 1966	+ 0.3	+ 3.4	— 0.6	+ 5.4	+ 8.9
4th. quarter 1966	n.a.	+ 0.4	+ 4.2	+ 6.4	+ 4.1

n.a. Not available.

NOTE: FTC-SEC figures on term loans to manufacturing corporations are on an outstanding basis, while the term loan figures reported by banks are based on original maturity. Changes in the FTC-SEC figures may be somewhat larger than they would have been if recorded on an original maturity basis.

Sources: *Quarterly Financial Report for Manufacturing Corporations,* FTC-SEC; Federal Reserve Bank of New York; Federal Reserve Bank of Cleveland

since it came at a stage of the business expansion when economic logic suggests that banks might have been unwilling to commit funds on a longer term basis. Thus, it may be in order to make some observations on the factors underlying supply-demand relationships for term loans.

The demand side of term lending is based upon the desire of businessmen to borrow funds for an intermediate length of time. The need for such funds stems from a variety of reasons, but two are probably most important: (1) the need to finance real capital (plant and equipment), inventories, accounts receivable, etc., and (2) financial strains that force a firm to borrow for more than a short time period.

The first of these reasons clearly accounts for the bulk of term loans. Demand for term loans to finance expansion of facilities and to provide working capital is generally thought to be closely related to the pace and direction of business activity. This suggests that demand for term loans would follow closely the contours of the business cycle, as well as businessmen's expectations regarding sales and profits.

The amount of borrowing by business firms is a function of both availability and price.

TABLE II

Percent Increases in Debt of Manufacturing Corporations, by Type

	Short-term	Term Loans	Other Long-term
1962	+ 3.9%	+ 7.6%	+ 6.2%
1963	— 0.7	+ 3.1	+ 6.0
1964	+10.8	+19.8	+ 4.7
1965	+29.8	+39.7	+11.3
1st. half 1964	+ 6.4	+ 1.7	+ 0.9
2nd. half 1964	+ 4.1	+17.9	+ 3.7
1st. half 1965	+16.4	+14.4	+ 5.2
2nd. half 1965	+11.3	+22.1	+ 5.7
1st. half 1966	+26.0	+16.6	+ 9.6
1st. quarter 1966	+ 9.3	+ 7.1	+ 5.2
2nd. quarter 1966	+15.3	+ 8.9	+ 4.2
3rd. quarter 1966	+ 7.7	+ 0.3	+ 4.3

NOTE: Term loan figures are on an outstanding basis while other FTC-SEC figures are based on original maturity. Changes in term loans may be somewhat larger than the other figures.

Source: Computed from FTC-SEC data

The form of such borrowing will depend largely on where funds are available, as well as on interest rates charged by competing sources of funds. A firm will raise money at a bank, in the capital market, or through other means, according to availability, relative costs, and expectations as to future costs. A firm may attempt to borrow at a bank for an intermediate period of time if long-term interest rates in the capital market are expected to fall; the latter situation would make a refinancing possible later, for a longer period of time and at lower cost. Some analysts attribute at least part of the acceleration in the demand for term loans at commercial banks during 1964-66 to this type of interpretation of credit conditions by business firms.

The demand for term loans should be expected to show some sort of cyclical pattern. For example, as the economy expands, businessmen usually borrow to expand facilities, and when the economy slackens, businessmen are more reluctant to borrow and often repay debt. Although interest rates usually rise during expansion, this will not necessarily curb the demand for funds if the business outlook is favorable and substantial profits are anticipated from planned investment. A major factor influencing the demand for term loans may be the desire to assure the availability of funds in a period of tightening credit. Relative interest rates will be more influential in determining where and in what form the funds are raised. The demand for term loans may increase despite the fact that the cost of such borrowing is increasing, if other rates are rising more rapidly. Similarly, a decline in interest rates during recessions will not necessarily encourage borrowing unless long-term profitability prospects are good.

The willingness of bankers to extend credit in the form of term loans depends on a variety of factors. One major factor is, of course, the supply of available funds, or the amount that banks have available to lend, that is, the banks' reserve and resource position. Other considerations include the requirements of portfolio distribution, the quality of credit (the soundness of the borrower and of his proposed project), the phase of the business cycle, relative interest rates, and bankers' expectations. For example, if the interest rate on term loans is attractive, bankers conceivably could make additional funds available for term lending by restructuring other assets and by channeling new deposits in this direction.

The supply of funds available for term lending would be expected to move countercyclically. Thus, as the business cycle ap-

proaches a peak with credit conditions becoming tighter (rising interest rates and slackened growth of bank reserves, bank credit, and the money supply), it would be expected that the supply of funds available for term lending would be reduced. Under normal developments, the opposite set of circumstances would be expected to prevail as economic activity is moving down. Factors limiting such a countercyclical pattern include the desire of banks to increase liquidity during periods of economic slowdown and to lessen liquidity in expansions, as well as the quality considerations associated with prospective customers and pressure to maximize bank earnings.

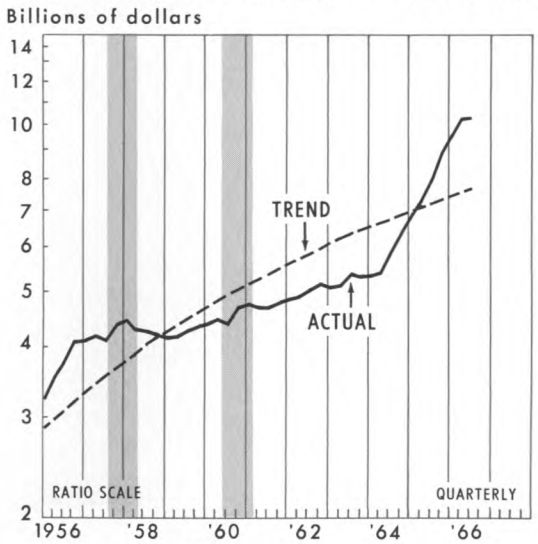
It might be argued that the supply of bank funds available for term lending would be expected to lead the business cycle, at least as based upon expectations regarding the movement of interest rates. Thus, as credit conditions become tighter and interest rates seem to be nearing a peak, the supply of funds available for term lending is likely to be small. On the other hand, if bankers feel the economy is close to or at a peak and that interest rates will soon fall, they may make additional funds available for term loans in an effort to lock in such loans at high interest rates, and thereby protect future earnings. Similarly, when the economy nears a trough and interest rates are expected to rise, funds may become less available for term loans as bankers restrict such lending until loans can be put on the books at higher interest rates.

TREND OF TERM LOANS

As illustrated in Chart 2, term loans have shown a fairly steady rate of growth over time, which is not surprising since a growing economy needs such financing to expand plant and equipment and working capital. (As shown in the chart, the straight line trend for term loans has a positive slope. The trend line was computed by the method of least squares, and was limited to the period 1956-66 since comparable data are not available for earlier years.) The spectacular growth in term loans beginning at mid-1964 contrasts markedly to the gradual but steady growth of the series over a longer period.

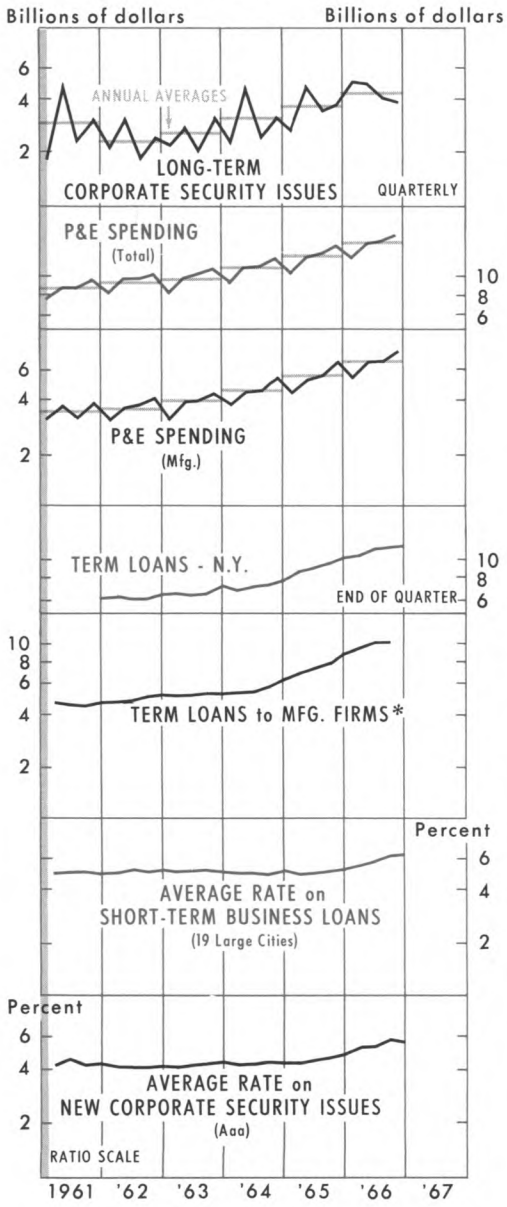
The relationship of term lending to manufacturing firms to the business cycle is also suggested in Chart 2, by a comparison of the computed trend for term loans with actual figures. While the chart suggests that there is no overwhelming cyclical pattern, it is clear that term loans to manufacturing firms tend to rise during economic expansions, for example, during 1956, 1959 to early 1960, and

Chart 2.
TERM LOANS to MANUFACTURING CORPORATIONS



Sources of data: FTC-SEC and Federal Reserve Bank of Cleveland

Chart 3.
SELECTED SERIES on BUSINESS SPENDING, BORROWING, and COSTS



*FTC-SEC Series

Sources of data: FTC- SEC; U.S. Department of Commerce; Federal Reserve Bank of New York; Board of Governors of the Federal Reserve System

1964 to 1966, and to level off or decline during recessions. In both the 1956 and 1964-66 periods, actual term loans were considerably above trend, as the chart shows.

ACCELERATION IN TERM LOANS

The 1964-66 boom in term lending reflected the interaction of supply and demand factors, but the latter seemed to dominate as the economy was in a particularly strong period of expansion. Substantial gains in the volume of term loans outstanding were perhaps to be expected, in view of the fact that a strong cyclical performance of the economy was superimposed on trend.

Chart 3 shows a number of selected economic series that have some relevance to term lending developments. Earlier in the current expansion capital spending by business firms had largely been financed through internal funds (retained earnings and depreciation allowances). This is reflected in the fact that the pattern of new corporate security issues was fairly stable during 1961-63. A step-up in business spending in 1964 necessitated the use of additional external financing, which to some extent was reflected in a rise in corporate security issues (see chart). It also resulted in an acceleration of term loans. As shown in the chart, term loans began to increase rapidly at about the same time as the rise in corporate security issues.

The general stability of interest rates during the early years of the current economic expansion was reflected in the behavior of short-term rates on business loans, which showed virtually no change from 1961 to the third quarter of 1965, and the rate on new

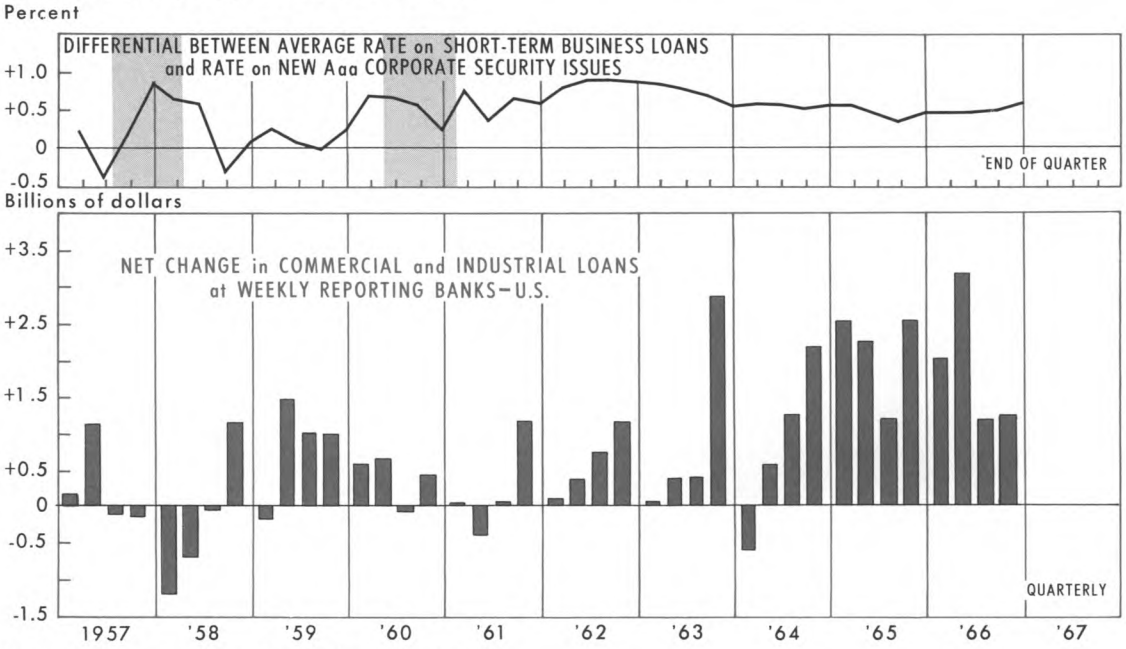
corporate issues, which did not begin to climb until early 1965. While data covering interest rates on term loans are not uniform and consistently reliable, the figures that are available indicate a pattern somewhat similar to that of short-term rates on business loans. Generally, it would seem that banks were able to accommodate the surge in term loan demand without escalating interest rates until late 1965, at which time the interest rate situation changed appreciably.

The increase in interest rates apparently did not radically reduce the demand for business financing, particularly the demand for term loans, but it may have had an effect on where such financing was obtained. The renewed surge in business activity and the acceleration of term lending at banks occurred at a time (1964-66) of relatively high interest rates in the capital market. More importantly, and as illustrated in Chart 4, the differential between the rate on short-term business loans at banks and the rate on new A a a corporate issues began to narrow appreciably in early 1963, with the latter rate edging up and the bank rate relatively stable. (The differential may be somewhat understated, because of increases in compensating balances at banks, which increase the actual cost of borrowing.) Even when the differential widened again in early 1966, bank borrowing still recorded sizable gains, which was probably prompted by the fact that the interest rate differential was not as wide as it had been in, say, 1962. Thus, the cost advantage implied by the differential apparently encouraged businessmen to borrow in the form of term loans for one or two years with the hopes of refinancing for a longer period in the capital market if and when open market rates declined. On the other hand, it may also be that businessmen did not expect rates to remain high, and wanted to commit themselves for a shorter time than they could in the capital market. And, as suggested earlier, bankers may have been willing to lend to good customers for longer periods of time, since it provided an opportunity to lock in loans at relatively favorable rates, at least from the banks' point of view.

Despite this, all demands for term loans were not accommodated. Banks to some extent were forced to "ration" the amount of such credit made available. The impact of rationing, to the degree it existed, is implied in the figures on who borrowed from banks in the form of term loans.

In Table III, percentage gains in term loans to manufacturing corporations classified by asset size are presented for the period 1962-66. The percentage gains that are significantly above the average for all asset sizes are identified in color. Smaller manufacturing concerns showed significant increases in term borrowing earlier in the current expansion (in 1962 and 1963). Term borrowing by medium-size firms predominated in 1964. But in 1965 and the first two quarters of 1966, the small- and medium-size firms (included in the FTC-SEC sample) clearly fell behind the large corporations, in terms of extent of increase in term borrowing. This suggests that the supply of term loans otherwise available to small- and medium-size firms was shifted in favor of large corporations. This conclusion is based on the assumption that the demands

Chart 4.
INTEREST RATES and BUSINESS LOANS



Source of data: Board of Governors of the Federal Reserve System

of small- and medium-size firms continued to be strong, which is not unlikely in view of the rapid pace of economic activity in 1965-66.

While this turn of events probably had some desirable effects, in that it restricted aggregate business borrowing at banks, it does indicate an immeasurable degree of credit rationing by banks when credit conditions tighten.[4]

[4] There are a number of articles in the economic literature that discuss this point. For example, see Marshall Freimer and Myron J. Gordon, "Why Bankers Ration Credit," in *The Quarterly Journal of Economics*, August 1965, pp. 397-416, and Thomas Mayer, "Trade Credit and the Discriminatory Effects of Monetary Policy," in *The National Banking Review*, June 1966, pp. 543-5.

CONCLUDING COMMENTS

Some of the foregoing may have value only as a contribution to experience, in that there are signs of a significant slowdown in the growth of term loans. Both the New York and Fourth District term loan series showed a slackening in the growth rates of such loans as 1966 progressed. Term loans at New York banks reached a high of 61.6 percent of total commercial and industrial loans at the end of the first quarter 1966; by the end of 1966 term loans accounted for 60.0 percent of total commercial and industrial loans. In addition, according to the FTC-SEC data, short-term debt owed to banks by manufacturing corporations increased more rapidly than either

TABLE III

Term Loans to Manufacturing Corporations, by Asset Size

	Percent Change from End of Previous Year					
	1962	1963	1964	1965	2nd. Q. 1966	3rd. Q. 1966
All Asset Sizes	+ 7.6%	+ 3.1%	+19.8%	+39.7%	+16.6%	+17.0%
Under $1 Million	+27.6	+19.7	+14.4	+ 8.7	+13.5	+17.3
$1 to $5 Million	+24.5	+11.7	+19.6	+27.4	+ 1.6	+ 5.2
$5 to $10 Million	+16.5	+23.8	+51.5	—14.9	— 3.4	+ 5.5
$10 to $25 Million	+21.2	+11.9	+32.8	+32.0	+ 4.7	+ 2.3
$25 to $50 Million	+ 5.5	+ 3.4	+26.0	+13.4	+ 8.5	+15.0
$50 to $100 Million	— 3.8	—29.2	+43.3	+55.5	+21.9	+18.2
$100 to $250 Million	+ 4.4	—19.6	+10.3	+33.2	+55.6	+65.3
$250 Million to $1 Billion	— 9.8	+16.0	+12.1	+82.0	+12.6	+13.2
$1 Billion and Over	+ 6.8	— 0.9	+11.9	+67.7	+22.2	+14.6

NOTE: Percentage gains significantly above the average for all asset sizes are identified in color.
Source: Computed from the *Quarterly Financial Report for Manufacturing Corporations,* FTC-SEC

long-term debt or term loans as 1966 progressed, and indications of credit rationing eased (see the third quarter figures in Table III). It remains to be seen whether the 1964-66 experience in term lending represented a fundamental shift in the nature of term lending, or instead was only a temporary deviation.

A NOTE ON BRANCH BANKING LEGISLATION AND BANKING STRUCTURE IN THE FOURTH DISTRICT

Earlier articles on the banking structure of the Fourth District have referred in a passing way to legislation that influences the structure of commercial banking in the Fourth District. Not surprisingly, the degree of "liberality" in the individual state's banking laws has influenced appreciably the types of changes that have occurred in commercial banking in the Fourth District since 1954. Since the Fourth District covers all or part of four separate states (all of Ohio and portions of West Virginia, Kentucky, and Pennsylvania), and since the banking laws of each of these states are different, it is necessary to consider each separately in order to understand the environment within which recent structural changes in District banking have occurred.

WEST VIRGINIA

In West Virginia, banking law prohibits the establishment and operation of branches within the state.[1] Thus, during 1954-65 the only changes that occurred in the banking structure of the Fourth District portion of West Virginia (comprising a six-county block in the Wheeling-Weirton area) were four mergers and three de novo starts. These changes resulted in a decrease in total banking offices from 25 to 24 over the 11-year period. Not surprisingly, West Virginia is the only state within the Fourth District in which the number of people served by each banking office has risen since 1954.

KENTUCKY

Prior to 1961, Kentucky banking laws allowed the establishment of branches throughout the county in which the main office was located, and permitted the establishment of branches in adjacent counties when the adjacent county had no banking facilities available to the public.[2] In 1962, the Kentucky banking law was revised to eliminate the

[1] See *West Virginia Code*, 1961, Section 3131.

[2] See Baldwin's *Kentucky Revised Statutes, Annotated* 3rd Edition, 1963 (including 1964-65 supplements), Title XXV—Business and Financial Institutions; Chapter 287—Banks and Trust Companies; Section 287.180.

privilege of branching into adjacent counties.

Although the new law permits banks to establish branches in the incorporated area in which the main office is located, banks cannot establish branches in other incorporated areas where there is a main office of another bank. The new law also provides that no branch can be established in an unincorporated area closer than one mile from the main office of another commercial bank. As a general matter, however, these revisions in Kentucky banking law have not seemed to hold back the steady growth of branch banking in the State. During the 1954-65 period, the number of branches in the Fourth District portion of Kentucky increased by 573 percent (from 11 to 74) while the number of banks decreased by 8 percent. The net result was a 31 percent increase in the number of banking offices in the portion of Kentucky that lies within the Fourth District.[3]

OHIO

In general, the law of Ohio restricts branches to the county in which the main office of the bank is located. Among the exceptions, there are a few instances where the city in which a bank is located is actually in more than one county, with the result that branches may be established in adjacent counties. In addition, there are situations where banks had affiliates before the branch banking law was passed in 1935 and were permitted to retain such banks as branches. Finally, there are isolated cases of out-of-county branches that are permitted under the law where the city in which the branch is to be located is contiguous to the city in which the main office is located but the two are actually in different counties. It should be noted in this connection that major revisions of the entire Banking Code of Ohio are being considered, and once these have been completed it may well be that the policy in Ohio in respect to branch banking may be reexamined.

County-wide branching in the State of Ohio has been conducive to rapid growth in the number of branches in operation. In 1954, for example, 637 banks operated 345 branches; by the end of 1965, through expansion and acquisitions, 542 banks operated 945 branch offices. The 174 percent increase in the number of branching offices offset a 15 percent decline in the number of banks, resulting in a 52 percent increase in the number of banking offices in Ohio.[4]

PENNSYLVANIA

In contrast to the unit banking law in West Virginia and the county-wide branching allowed in Kentucky and Ohio, the State of Pennsylvania, through its revised banking code, permits branches to be established in the main office county and in any county contiguous to the main office county. Prior to 1955, establishment of branches in contiguous counties was conditioned upon documentary evidence that the contiguous

[3] For further information on changes in the banking structure of Kentucky, see "The Anatomy of Fourth District Banking, 1954-65," *Economic Review*, Federal Reserve Bank of Cleveland, Cleveland, Ohio, May 1966, pp. 3-12.

[4] For further information on changes in the banking structure of Ohio, see "The Anatomy of Fourth District Banking, 1954-65," *op. cit.*

county was without adequate banking facilities.[5] In the revised banking code of 1955, the adequate banking facilities test was eliminated.[6] Since that time branch banking in the State of Pennsylvania has flourished, with the number of branches rising from 154 in 1954 to 455 at the end of 1965—a 196 percent increase. The more liberal branch banking provision of Pennsylvania law has probably contributed importantly to the decline in the number of banks in Pennsylvania, which has taken place primarily through merger and consolidation. The new banking code of 1965[7] retained the provision for branch banking in contiguous counties, and will make possible further sizable changes in the banking structure of Pennsylvania.

[5] See Purdon's *Pennsylvania Statutes, Annotated,* 1954, Banking Act of 1933, Section 819.204, repealed April 27, 1955.

[6] See Purdon's *Pennsylvania Statutes, Annotated,* Title 7: Banks and Banking, Section 819.204.1, effective April 27, 1955.

[7] See Purdon's *Pennsylvania Statutes, Annotated,* "Pennsylvania Banking Code of 1965," Title 7: Bank and Banking, Section 904.

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