1952

Financing the development of Industry in Arkansas

Arthur P. Thompson
University of Arkansas, Fayetteville

Follow this and additional works at: http://scholarworks.uark.edu/jaas

Part of the Finance Commons, and the Regional Economics Commons

Recommended Citation
Available at: http://scholarworks.uark.edu/jaas/vol5/iss1/19

This article is available for use under the Creative Commons license: Attribution-NoDerivatives 4.0 International (CC BY-ND 4.0). Users are able to read, download, copy, print, distribute, search, link to the full texts of these articles, or use them for any other lawful purpose, without asking prior permission from the publisher or the author.

This Article is brought to you for free and open access by ScholarWorks@UARK. It has been accepted for inclusion in Journal of the Arkansas Academy of Science by an authorized editor of ScholarWorks@UARK. For more information, please contact scholar@uark.edu, ccmiddle@uark.edu.
FINANCING THE DEVELOPMENT OF INDUSTRY IN ARKANSAS*

ARTHUR P. THOMPSON

University of Arkansas

One of the traditional deterrents to industrial development is a shortage of local money capital for the purpose. Arkansas is by no means unique in this respect. Preliminary study indicates that the shortage here is more acute than in the more highly developed industrial states.

In the case of industry native to Arkansas, the problem is primarily one of financing new and expanding small firms. Small firms everywhere have more difficulty in securing funds than do their larger competitors. The larger firms, of course, have access to the capital markets of Wall Street and elsewhere. Small firms traditionally depend on local sources for the bulk of their funds since outsiders are seldom in a position to know or care about the prospects of success of the small venture.

Small firms experience special difficulty in obtaining equity capital. Their sources for this risk capital are usually confined to the savings of the proprietors, their friends, relatives, and business associates, and to retained earnings. Such firms are not in a position to issue securities on a large scale. They are often reluctant to tap even all of those sources of equity capital which are available lest control of the firm should become divided.

Even aside from the issue of control, it must be remembered that the principal source of funds for small firms, the commercial bank, is not in a position to advance equity capital. Most small firms, keeping in mind their desire to retain control of the firm in the hands of the original proprietors, would be quite willing to settle for long-term loans. Here again, however, the activity of the commercial banks is limited. There has been a tendency in recent years for banks to look with increased favor on longer-term loans. It is unlikely, however, that the desires of small business for loans of duration comparable to that of the bonds issued by larger firms will be met by commercial banks. This emphasis by commercial banks on short-term loans is apparently unavoidable. Banks must maintain liquidity for the protection of their depositors, most of whose funds are placed in the banks on a demand basis.

Although difficulties are encountered by small firms everywhere, they are particularly acute for small manufacturing firms in a region, such as the South, whose economic background is predominantly agricultural and commercial. In such regions the average person with savings to invest is less likely to think of putting those savings into a manufacturing enterprise. Such savings usually go into real estate, banks or other financial institutions, or securities issued by governments or large national corporations.

Commercial bank loan policy is also influenced by the economic background of a region or community. Bankers who deal primarily with agricultural and commercial loans become expert at evaluating and servicing such loans, and are more reluctant to handle the comparatively unfamiliar needs of manufacturing.

The problems previously discussed apply especially, although not exclusively, to small manufacturing firms native to the State. The financial problems involved in inducing large out-of-state firms to establish branch plants in Arkansas are different. These firms usually have less difficulty in obtaining the bulk of their financial needs. With the small native firms the problem is to expand at all. In the case of larger outside firms the question is more likely to be where to expand.

As part of a general program designed to promote industrial development, many communities have established some kind of organization to render financial


* * Research Paper No. 1041 Journal Series, University of Arkansas.
assistance to industrial firms. These organizations ordinarily raise money from local businessmen, who expect to profit only indirectly, through increased sales resulting from prosperity generated in the community by increased employment. Financial assistance rendered to industrial firms by these foundations typically consists of the provision of a plant at reduced or nominal cost. Firms utilizing the assistance of such foundations are usually larger out-of-state concerns which have already decided to expand. The help rendered in providing plant space is designed, along with other promotional activities, to make the community involved the most attractive site for such contemplated expansion. Aside from the financial assistance thus rendered (which, nationally speaking, has not been large), these community industrial development foundations are useful as an indication of community support for industrialization.

Presumably these large outside firms locating branch plants in Arkansas will continue to obtain the bulk of their required funds from the national capital markets. Small firms native to Arkansas, on the other hand, must rely largely upon investment by Arkansans. This investment, in turn, is dependent upon savings, income, and the general prosperity of the State. Two indices of such conditions may be useful in appraising the State's economic progress.

Per capita income in Arkansas increased from $305 in 1929 to $778 in 1949. This represented an increase of 155%, compared with the national average increase of 96%. The dollar figure for Arkansas is still well below the national average of $1,330, indicating that there remains much room for improvement.

Deposits by individuals, partnerships, and corporations with Arkansas banks amounted to $608,265,000 in 1950, compared with a total of $130,041,000 in 1939. This represented an increase of 368%, as compared with a national average increase during the same period of 196%. The approximate 1950 per capita figures were $320 for Arkansas and $768 for the nation as a whole.

The few statistics above are in substantial agreement with most indices of the prosperity of Arkansas as compared with the nation as a whole. Such indices generally indicate that Arkansas compares unfavorably as to present conditions, and favorably as to rate of improvement.

It is not possible to determine from the above statistics the exact amount of savings which might be made available for investment in industrial expansion within the State. It is apparent, however, that a substantial portion of the desired expansion of native Arkansas industry could be financed from the savings of Arkansans. These savings are at present not being fully utilized for this purpose.

In 1947, the latest year for which figures are available, expenditures for new plant and equipment in Arkansas amounted to approximately $30.3 million. This compared with a figure of $4.4 million for the year 1939. This seven-fold increase compared with a five-fold increase for the nation as a whole. Value added by manufacturers in Arkansas increased from $66,444,000 in 1939 to $265,144,000 in 1947. This increase of approximately 290 per cent compares with a national average increase of 204 per cent.

Such expenditures in Arkansas in 1939 represented approximately 0.9 per

2For a brief analytical survey of such organizations see: Thompson, Arthur P., "Plans For Financing Local and Regional Industrial Development", Arkansas Business Bulletin, April 1951, pp. 1-6. (Published by University of Arkansas, Bureau of Business and Economic Research)


4Federal Deposit Insurance Corporation, Reports of assets and liabilities of insured banks, as of June 30 of each year.


6Source: U. S. Census of Manufactures.

7Ibid.
cent of the State's income\(^8\) as compared with a national average of 1.8 per cent. In 1947, the figure for Arkansas was 2.2 per cent, and that of the nation 3.2 per cent.\(^9\)

These statistics furnish some indication of past progress. Prospects of future progress may be judged by the attitudes and activities of persons in the State. Activities of numerous organizations in the state reflect a desire to encourage industrial development. These organizations include the Arkansas Resources and Development Commission, State Chamber of Commerce, Associated Industries of Arkansas, utilities and other business firms, and various local groups. Several Arkansas communities have organized industrial development foundations to provide plant space for industry.

No current discussion of industrial development would be complete without reference to the war production program. The scale and duration of this program are, of course, not yet known. It is clear, however, that the scope of war production is such as to exert an overwhelming influence on the types and amounts of industrial development which may be expected to take place in the next few years. The nature of the program leaves considerable room for promotional activities by Arkansans. Although Federal government policy exerts some influence on plant location, the decisions generally are made by individual firms, before government contracts are secured.\(^10\)

The position of the Federal government in regard to financing of war plants today differs substantially from that in the early days of World War II.\(^11\) This may be due largely to the fact that the prevailing view of the capability of American industry to meet war production needs is much more optimistic today than a decade ago.

During the last war, the government felt it necessary to finance much of the expansion from federal funds, rather than to ask private enterprise to take excessive risk of possible future losses due to war-induced expansion of productive facilities in excess of normal needs. Most of the financial encouragement along this line today consists of more liberal federal corporate income tax treatment. Specifically, the cost of certain production facilities may, for corporate income tax purposes, be charged entirely to depreciation over a five-year period. The amount of expansion costs which may thus be "depreciated" is contingent upon obtaining from the Defense Production Administration a "certificate of necessity", certifying that the facilities involved are vital to the defense effort. The President has directed that the DPA be lenient in granting such certificates.

Some provision has been made for Federal loans, through the Reconstruction Finance Corporation, to enable firms to expand to meet war contract commitments. The number of such loans, however, has been, and is expected to continue to be, much smaller than in World War II. Under present policies, in other words, the overwhelming majority of war production facilities must be financed without benefit of loans or advances from the Federal Government.

CONCLUSIONS

1. In attracting branch plants of outside industrial firms, financial problems are not of prime importance. Community industrial foundations, can, however, be useful in attracting such industry.

\(^8\)Income figures: Total income payments to individuals; compiled by U. S. Department of Commerce, Office of Business Economics; Survey of Current Business, August, 1950, p. 19. Figures for expenditures for new plant and equipment obtained from U. S. Census of Manufacturers. It should be cautioned that such figures represent expenditures in Arkansas, rather than by Arkansans. It is impossible to determine from existing information what percentage of Arkansas income is actually invested in Arkansas industry.

\(^9\)The percentages for the neighboring state of Louisiana in both years were approximately double those for Arkansas.


\(^11\)Ibid.
2. In the case of industry native to Arkansas, financial problems are of greater importance. The crucial problem here appears to be provision of equity and long-term loan capital for new and expanding small firms.

3. The problem of channeling local funds into industrial development in Arkansas appears to be aggravated by the economic background of the state. A sharp increase in investment by Arkansans in the development of native industry may probably be expected only with a change in the economic climate and financial attitudes.

4. It might be desirable to finance all of the projected industrial development without "importing" capital into Arkansas and "exporting" profits. The desired rate of industrial expansion, however, will almost certainly require considerable outside financial assistance.

5. Such indices of prosperity as income and savings data generally indicate that Arkansas compares unfavorably with the nation as a whole as to present conditions, but favorably as to rate of improvement.

6. The activities of numerous organizations and agencies within the State indicate considerable interest in industrial development. Actual expenditures for new plant and equipment are less encouraging.

7. The present war production program presents an opportunity for acceleration of the State's industrial development. Most of the actual financing of this development, however, must be done without direct federal assistance.