THE ENVIRONMENT FOR SMALL BUSINESS AND ENTREPRENEURSHIP IN REGION IX

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THE ENVIRONMENT FOR
SMALL BUSINESS
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Sponsored by
Small Business Administration
Washington, D.C. 20416

Research Contractor
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THE ENVIRONMENT FOR SMALL BUSINESS AND
ENTREPRENEURSHIP IN SBA REGION IV

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ENTREPRENEURSHIP AND SMALL BUSINESS
IN THE SOUTHEAST: A SUMMARY VIEW

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1. INTRODUCTION

This essay summarizes the contents, conclusions, and recommendations of twenty papers about small business in the Southeast, or Federal Region IV, including North Carolina, South Carolina, Georgia, Florida, Alabama, Mississippi, Tennessee, and Kentucky. Located at universities and research institutes throughout the region, the authors reveal a considerable diversity of opinion as they record and interpret facts and feelings about the environment of small business in the Southeast. They have been restricted only by their choices of topics and by a requirement that they write about small business as defined by the Small Business Administration. We have edited primarily for style and consistency in presentation, and have published all of the essays commissioned. In almost every case, the authors have collected a considerable amount of original data and have used great care and skill in analyzing it. The papers tell us much regarding the attitudes and needs of small businessmen themselves. We should note that the conclusions do not necessarily represent the opinions of the Small Business Administration, The Chair of Private Enterprise, or the editors.

The papers may be classified into seven groups. Two papers describe the economic history and a current profile of small business in the Southeast. Three papers outline the entrepreneurial resources of the region. Three case studies of major industries yield insights into the roles of entrepreneurs and into the specific needs of small businesses. Five papers
concentrate on the impacts of government regulations, policies, and agencies on small businesses and yield a lengthy series of recommendations. One paper explores the sources of credit and venture capital in the Southeast. And six papers discuss the problems, needs, and opportunities facing small businesses. The summaries which follow are organized to express these groupings. We have attempted to extract and highlight the major points of each essay.

2. SMALL BUSINESS IN THE SOUTHEAST

The volume begins with two essays on the development and status of small business in the Southeast.

An Economic History

Jack Blicksilver has written a stirring economic history of small business in the region which defies any attempt at summarization. He describes the early influence of the mercantilistic policy of Great Britain, of a good climate, and of plentiful resources on production of primary products, and then carries the region through the 19th century, when commerce served as the handmaiden of agriculture, showing both the influence of the frontier experience in the western part of the region and the effect of the region's long reliance on a dependent labor supply. He vividly depicts the development of cotton mills after the Civil War as a happy marriage of native capital and entrepreneurship. And he records the severing since World War II of the region's links to a stagnant past as the Southeast has moved into the economic mainstream of the nation. Little is left unobserved as Blicksilver ferrets out the determinants of the current structure of the region's economy.

He concludes with a current profile of small-scale enterprise.
An Economic Profile

Carole E. Scott develops a more extended profile of small business in the region. She looks at firms with up to 500 employees and finds small business more important in the region than in the nation as a whole. Her data base points out the strength of small business in manufacturing and construction in the region. In fact, both Blicksilver and Scott associate the region's economy with small business.

3. ENTREPRENEURIAL RESOURCES IN THE REGION

Three of the papers take a look at recent entrepreneurs in the region, reviewing the characteristics of women and minority members who own small businesses, the government actions which would enlarge the ranks of minority businessmen, and the origins of entrepreneurs who develop technology-based enterprises.

Profiles of Women and Minority Persons

Dale L. Flesher and Kenneth W. Hollman provide profiles of women, the elderly, and minority persons in small business. Using a series of personal interviews, they develop some interesting contrasts. Although long discouraged by the socialization process, women are going into business in increasing numbers. Husbands and other males were given credit for encouragement by 90 percent of the sample of women (males seldom gave credit to anyone), who also mentioned their children (an average of 2.3) as reasons for entering business. Females start businesses about four years later than males, but both male and female entrepreneurs establish their firms about the same age of 35. Only 76 percent of the women were married, as opposed to 97 percent of the men. The average white male entrepreneur had held two managerial positions before entering business, and the average female only one. While white men were
more likely to have attended college and graduated, females were more likely to have majored in business in college and to have acquired a graduate degree. And while white males typically started as unskilled workers, women were more likely to have started as clerical or sales workers.

Minority owners had definite goals in going into business for themselves, most often wishing for a feeling of independence and showing a desire for a better life for themselves and their families. While white owners typically had fathers who owned small businesses, the fathers of minority owners were unskilled workers or farmers. College was also important for minority owners, with almost half of them holding bachelor's degrees and 15 percent earning master's degrees (in contrast to 5 percent of white men). Minority members also had more experience in the armed forces and were more likely to have been born in the large city in which they established their business.

The Role of the Minority Entrepreneur

Gerald F. Whittaker further explores the role and importance of minorities in the region. He contends that minorities in the American economy, and especially in the South, suffer in large part from economic deprivation and social degradation. Using the minority-owned business as his statistical unit, he points out that minority-owned firms represent less than 5 percent of all U.S. businesses, obtain only 0.7 percent of business receipts, and provide employment for approximately 0.8 percent of the labor force. With minorities comprising 18 percent of the population, he finds this disturbing. In this region, which has a higher concentration of minorities, it becomes especially disturbing, with minority-owned businesses comprising 8.8 percent of the total and receiving only 0.6 percent of total income.

In a review of recent changes, he finds a dramatic increase between
1972 and 1976 in the number and receipts of minority-owned firms in construction and selected services, reflecting provisions for minority participation in Federal contracts. But in 1979 a decline of Federal funding for the Office of Minority Business Enterprise and the phasing out of the Local Public Works Procurement Program, brought a decline in assistance and in marketing contracts for minority enterprises. In a review of economic conditions, however, he maintains an optimistic position, and proposes hard-hitting courses of action in three programs directed at the entrepreneur, at capital, and at markets.

Whittaker sees minority professionals in business-development organizations as a source of entrepreneurs, and proposes to encourage them to become entrepreneurs through both financial assistance and a limit of five years to their tenure as bureaucrats. Minority managers in majority-owned firms should also be induced to seek ownership of anti-trust divestitures and of medium-sized businesses which are for sale. And with government and foundation support, universities should see that minority persons comprise 20 percent of their business-school graduates, and majority-owned businesses should have business-internship programs for minorities.

For the capital with which to fund minority enterprises, Whittaker proposes a program of government deposits in minority-owned financial institutions and the favoring of majority banks which lend to minority businesses with additional deposits. He also proposes employee stock ownership plans in the private sector, with minority management, but places heavy emphasis on government action, both in direct loan programs and in encouraging pension funds by giving tax exemptions for investments in minority enterprises.

For market development, Whittaker proposes substantial government contracts for minority firms, assistance in identifying market opportunities
by minority business development organizations, assistance in recruiting minority management personnel, and assistance in identifying business-acquisition opportunities and in financing these acquisitions. He also suggests a first offer by the government to minority firms of the fruits of space research and other high-technology programs.

Whittaker concludes his polemic with a strong note that "only government can perform on the basis of a social conscience. ... Years of deprivation and continued discrimination have left minorities without the asset base for meaningful business development through their own efforts. Significant government action is desired."

The Technological Entrepreneur

Marilu McCarty focuses on yet another source of entrepreneurship, the university. In particular, she looks at small businesses based on high technology and which may be classified as "spinoffs" from the Georgia Institute of Technology. Using series of interviews with eight high-technology firms, she finds entrepreneurial traits similar to those reported by Flesher and Holman. The entrepreneur is likely to be in his or her thirties and to have strong motivation: the desire to achieve, to be one's own boss, and to respond to challenge. Only one entrepreneur named a role model.

Most of these technological entrepreneurs expressed some dissatisfaction with their experience at Georgia Tech, feeling that institutional limits inhibited aggressive leadership and helped to preserve a provincial attitude toward new developments. A policy conclusion could be drawn: regional progress through small-business development could be promoted by attracting aggressive, energetic research scientists and engineers to employment in a limiting situation from which their frustrations would lead them to eventual private
entrepreneurship! Nevertheless, the older firms expressing these views felt that early support by the Institute would have enhanced their potential for success.

Outside financing was minimal for most of the spinoff firms, although some had used venture capital and development-bond sources for their money. Aside from financing, the most commonly expressed need was help with marketing.

In general, the entrepreneurs, despite their attitude of independence, felt that the Institute could serve more effectively as a hub of technical resources if it would adopt an attitude toward spinoff activities which reflects more the "umbrella" than the "proprietary" way of thinking.

McCarty's findings regarding the Small Business Administration were generally positive. The SCORE and ACE programs were rated as helpful. The Technical Assistance Program was mentioned as valuable but not sufficiently publicized. None of the firms interviewed had obtained SBA loans, citing red tape and a minority focus as obstacles. They suggested earmarking a portion of Federal contract money for small research firms, perhaps with a university or other such center matching contracts with the capabilities of small businesses.

McCarty concludes that the common thread in the comments of these entrepreneurs is "... the drive toward application—toward responding to a perceived need by adoption of new technology. Most of all, they want vehicles for communication: among themselves, with experts ..., with potential users of their services."

4. INDUSTRY STUDIES IN ENTREPRENEURSHIP

The rise of the region as a significant force in the carpet, furniture, and agribusiness industries is traced in three papers. These papers address
themselves not only to the development of these industries but also to an
analysis of their current and future problems and to recommendations for
action by both the government and the industries.

The Tufted-Carpet Industry

Dan H. Robertson provides a review of marketing practices of the carpet
industry in the region. Approximately half of the tufted-carpet output of the
United States originates in Dalton, Georgia, which has over 150 carpet-producing
mills and is the home of the Carpet and Rug Institute. The growth of this
industry in this location offers an ideal example of the effect of entrepreneurial
fever and small business on a small town. But Robertson's concerns are with
current marketing practices in the industry and with the need for marketing
audits in the industry.

Current marketing practices are weak, and Robertson provides an
interesting review which may be briefly summarized. Carpet is a product in
the early stages of maturity with a forecast of slow but continual growth
over the next few years. Having many small producers who have established
little product differentiation, the industry is characterized by intense
price competition. The industry itself has done little consumer education,
marketing strategies are weak, and little market segmentation has taken place.

To provide a basis for correcting these weaknesses in a
production-oriented industry, Robertson suggests that both the industry and
its firms should conduct marketing audits based on the answers to five
simple questions. (1) Who are our customers? In many uses, carpeting is an
intermediate product, with the "true" customer, the user, at the end of a
long line of middlemen. Knowledge of the customer is an essential basis for
a useful marketing strategy. (2) Why do our customers buy our product/service?
Research studies have shown that appearance (primarily color or pattern) was
the most important factor considered by consumers, while price appears to be
the most advertised factor. Continued market research is essential in
answering this question. (3) What are we selling? Is carpet simply a floor
covering, a lifestyle, a room warmth? Can the product be more strongly
differentiated? (4) Who are our competitors? In Region IV, the vast
majority of producers consider their competition to be other carpet and rug
producers in the region. But this is short-sighted, to say the least; given
current import and export statistics, the competition should also include
other producers, both in the U.S. and in foreign countries. Further, it
might be extended to producers of paint products, wall murals, wall coverings,
tiles, other hard-floor coverings, etc. And (5) How do our target markets
view us relative to competition? In approaching this question, Robertson
emphasizes the critical words, "relative to," and calls on the carpet producer
to view his product comparatively, as would a potential consumer.

On the basis of his own answers to these questions, Robertson makes	hree specific recommendations for enhancing marketing practices in the carpet
industry. First, the industry must do something to increase its potential.
New products, such as the recently developed artificial-grass carpeting, must
be exploited along with new markets, including the little-explored export
market. In addition, the industry could further increase its efforts in areas
currently dominated by competition, such as the hard-surface floor covering
industry.

Second, the carpet industry could extend its current consumer
education efforts to include technical training for more retail sales personnel
as well as more advertising and informative materials aimed at consumers. And
third, producers must seek to obtain further product differentiation. Growth
in the housing market and in construction have provided the bases for dramatic
sales increases in the past. Now, the industry can no longer afford an undifferentiated product.

The important thing about Robertson's article is that it not only offers recommendations for the carpet industry but it also provides a lucid guide to marketing audits for the small businessman in any industry. His description of the marketing auditing process within a growth industry is worthy of careful review by the small businessman.

The Furniture Industry

James E. Littlefield has provided an excellent review of small business (firms with less than 20 employees) in the furniture industry in the region. With 286 furniture establishments in 1977, North Carolina has the largest furniture production in the nation for several reasons: softwoods for inexpensive furniture are plentifully available there; wages are relatively low; and High Point became the major furniture market center in an industry which is forced by high transportation costs to have a central place at which distributors may view the product.

Littlefield contends that the problems of small business are the same as those of large ones, only larger. Small firms, with less flexibility and fewer resources, find problems more difficult to solve. Based on discussions with furniture manufacturers, he identifies five major problems.

Lack of management skills is the most general problem. This is especially true of industries which are easy to enter, as is the furniture industry, and for which rapid growth based on a single customer is possible.

A second major problem is a lack of marketing expertise. Most often, the business originates with a person who is most familiar with production and whose knowledge of distribution, promotion, and pricing is small. Such persons are not prone to carefully analyze possible alternative distribution
channels and may find considerable and unexpected competition at an inopportune time.

Finance is the third major problem, especially in a business which depends heavily on factoring. To compound matters, small furniture producers often have to deal with sales outlets with credit ratings which are less than ideal.

Inventory control is the fourth major problem. Small businesses especially have trouble assembling expensive raw materials quickly enough to fill orders promptly without incurring excessive inventory costs.

And the fifth major problem identified by Littlefield is government regulation, which is much more of a burden to small firms than to large ones. The limited management of small firms has difficulty in understanding which regulations apply and how they apply. Further, small firms often lack the technology required to meet regulations. And some simply ignore the regulations until they are caught, making compliance doubly burdensome.

Recordkeeping is a related problem for small operators, who, as people of "action," have neither the skills nor the will to maintain good records.

Littlefield makes several recommendations for government action. Consulting help could be provided to small producers. These consultants should be fewer in number (one good all-around consultant is worth ten specialists). They could help with long-range planning, with money management systems, and with manufacturing and office systems and procedures.

His second recommendation regards information. The SBA and other government agencies should provide more information on available assistance, including more, clearer information on the types of business and the persons eligible for SBA loans. The misconception that SBA exists only to lend to minority businesses should be corrected by publicity and action. And the SBA
could improve its loan-guarantee program by better informing banks as to its nature, by developing better selection criteria, and by improving application procedures.

His third recommendation is that a moratorium on certain taxes and regulations for a period of two to three years could be granted to help new small businesses through the period in which they are becoming established.

**Agribusiness**

James R. Miller has produced an essay showing the development of agribusiness based on technological changes initiated by both large and small businesses. Since World War II the technology of farming and food processing has changed dramatically, and the Southeast has recaptured a significant place in the industry. But scale of production has changed significantly and farming has become big business.

For potential small businesses in agribusiness, Miller's outlook is negative. "... With agribusiness being very mature, with growth slowed or declining, with market shares established, and with capital and management well-positioned, the situation is one of very limited opportunities for new entrants, particularly small businesses."

5. **REGULATIONS, TAXES, AND GOVERNMENT POLICIES**

Although most of the papers in this volume are concerned with some aspects of government policies, five are specifically devoted to them. Almost all of these are critical. Tax regulations hinder and discriminate against small businesses. Downtown districts and their businesses should not depend on the Federal government for aid in surviving financially; the government should concentrate its attention on contributions which help build a sound economic base. Federal regulations in general handicap small businesses and
should be more carefully established. State and local governments could improve their development efforts by concentrating on local ventures and their needs instead of emphasizing relocation of branch plants. And a study of determinants of Congressional votes emphasizes economic inefficiency of legislative intervention.

**Taxation and Small Business**

K. Mark Weaver reports the tax-related concerns of small businesses as derived in an extensive survey of small businesses in the region. With over 1300 responses from a 5000-firm sample, he has gathered a representative sample of attitudes toward taxes. His article only begins to exploit this vast data base, but it does provide significant insights into the tax-related attitudes of small businessmen. These attitudes primarily concern simple survival as a business under a tax burden, gathering of the resources required for expansion, and complying with an increasingly complex set of regulations.

Firms in the sample feel that tax policies attract new equity capital into capital-intensive investment opportunities and away from the more labor-intensive, and possibly more risky, small businesses. And with survival often depending on accumulating capital, these firms feel biases with respect to other sources as well: borrowed funds come at higher costs for small businesses, and the heavy interest burden makes small businesses even more susceptible to failure during recessions; for small businesses which are capital-intensive enough to benefit from depreciation schemes and investment tax credits, remains the task of assembling the battery of accountants, lawyers, and tax consultants required to understand the complex array of tax laws; and, with respect to retained earnings as a final source of capital, small businesses feel that they face higher effective tax rates than do larger ones.
But the major complaints of small businesses were lodged against the payroll tax on three points. First, simply paying the tax is onerous enough, but the pain is compounded for small firms with high turnover rates, since a multiple tax liability is incurred on positions suffering high turnover. Second, complying with reporting requirements at frequent intervals is a problem in itself. And third, the determination of employee status is a major concern. Since no employer payroll taxes are payable for persons who are self-employed independent contractors, and since small businesses are typically more labor-intensive, small businesses waste a great deal of time with the subjective considerations involved in determining who is and who is not independent and in defending these decisions.

The complexity of the tax system and the associated paperwork also affect small businesses more than others. Small firms cannot maintain the staff of experts required to master the system and suffer higher costs in buying expert advice and in diverting entrepreneurial energies to face picky administrative details. Weaver lists over 25 filings required of most small businesses in Alabama on at least an annual basis.

A final major source of inequity facing small businessmen is the difference in treatment of retirement and fringe benefits for corporations and for proprietorships and partnerships. The corporate form of organization generates much greater pension and profit-sharing plan deductions than does a non-corporate form; in addition, it may deduct many of the fringe benefits provided to employees as business expenses, while the non-corporate form may not.

With 1300 responses to his questionnaire, Weaver obtained an almost unlimited supply of candid suggestions. He extracts their flavor on three points: reduction of taxes, simplification of paperwork, and provision of incentives and credits. Among their detailed recommendations are the
following. Reduce taxes, specifically payroll taxes and their reporting requirements. Stop using only lawyers to finalize tax regulations. Think about the impact of regulations on firms. Require "tax impact" studies to determine the full cost of compliance. Provide a "no-fault/no-risk" tax advisory service for small firms through which they can discuss problems without risking a penalty or jail term with no chance to correct the situation. Simplify depreciation rules. Adopt a cash accounting system for tax purposes. Adjust capital-gains rebates to reflect risk differences due to size. Allow reinvestment with deferred taxation. And more.

Federal Assistance and Downtown Businesses

Neil Snyder and Joe Burnett review the effects of Federal laws, regulations, and programs on small downtown business, especially as seen in their effects on local government revenues. In addition to their own knowledge of Federal assistance programs, Snyder and Burnett use 14 responses to a questionnaire mailed to the mayors of 83 cities in the region. If these few responses are typical, city governments in the Southeast show an increased reliance on the Federal government for financial assistance rather than for help in building a solid economic base.

SBA loans and guarantees received the most attention as devices through which marginal and troubled firms could survive or overcome crises. The Community Development Block Grant Program, the historic preservation allowances of the Tax Reform Act of 1976, and Urban Development Action Grants received mixed comments as to their effects on downtown areas and businesses. As Snyder and Burnett point out, however, the importance of the responses lies in their focus on federal subsidies for improving existing conditions and in their ignoring of incentives for increasing or stimulating private investment.
Snyder and Burnett close their critique with comments on the philosophy of government assistance, noting that the Federal goal should be not a reworking of Federal programs to resolve conflicts, but an elimination of many programs. "When someone helps open the cocoon, the butterfly dies because it misses the chance to use and develop its own muscle." They encourage private and local initiative in solving the problems of downtown businesses.

The Financial Effects of Regulation

Marvin E. Ray reviews the impact of Federal regulations on small business in general. The end of World War II marked the beginning of 25 years of economic progress during which investments were capital-intensive, labor-saving, and energy-intensive. With increased fixed costs, higher levels of output were required to break even. And with the end of cheap energy in the 1970s, variable costs increased to push breakeven output even higher.

With progress came regulation. Ray points out the range of regulations faced today and explores their financial implications. Since most expenditures required by regulations are nonproductive, their effect is to reduce profitability. In addition, they subject the firm to "legislative risk" and to uncertainty in interpretation. The financial effect of regulations which reduce profits and increase risks is a reduction of debt capacity for the firm.

Ray derives several implications for government policy makers. First, they should be aware of the importance of preserving the financial integrity of the firm. Second, they should recognize that the regulations posted by their agency are only one set among the many imposed by government agencies and should attempt to view their regulations from the point of view of the
firm, which faces a multitude of often-conflicting demands. And third, economic impact statements for regulations should go beyond their historical perspective. They should concentrate on such issues as inflation, productivity, capital formation, and innovation; they should consider conflicts between federal and state regulations; and they should focus on the financial impact of regulations in terms of return, risk, and debt capacity of the firms to which they will apply.

State and Local Government Influences on Small Business

Kenneth C. Wagner brings his substantial experiences in regional development in Mississippi and Georgia to bear on the question of state and local government practices that affect small business. First, he sets out a series of important things not done by state and local agencies, especially in Mississippi. The major cause of business failure, according to Wagner, is a lack of planning. When it is apparent that a business is poorly conceived, development agencies should act to prevent its birth until an adequate review and rethinking can be completed. This negative approach is seldom taken. Most state development agencies fail to act as information centers for small businesses. Local governments fail to assist with planning of facilities, they often provide inadequate zoning, and they turn deaf ears to pleas for assistance in land acquisition. Local political problems, often personal and petty conflicts among public officials and businessmen, slow business growth. Tax policies may discriminate against the local entrepreneur in favor of the "blue chip" branch plant. Small-business financing agencies established to take risks become too conservative. Vocational training programs ignore the skills most needed by local producers. Development agencies fail to maintain skills-data banks to assist in finding manpower ready to settle in the community in response to a job offer. And state agencies fail to provide
a wide range of information services at places easily accessible by small businesses throughout the state.

Wagner argues that the economic value of small businesses makes these omissions and failures significant. Half of new jobs in recent years in most states have come from expansions, and at least a third to a half of these can reasonably be attributed to the expansion or establishment of small businesses. He contends that the long-run interests of an area are better served through tax revenues devoted to helping with expansion of existing ventures and the development of new ones through local entrepreneurs than through tax dollars funneled into the search for new and increasingly scarce relocations of branch plants.

Wagner concludes his essay with a look at some state and local government options. One is the establishment of one or more types of financing agencies. He offers two cautions about such agencies: they are often under-financed, and they become so extremely conservative that they often miss their best opportunities. Another option is a state technical service to perform a technical-economic evaluation of ventures for which funds are sought. A third is a training program for potential and operating entrepreneurs to help in overcoming such critical early problems as cash-flow deficiencies, tax planning, financial management, sales, marketing, etc. A fourth option is a sound "Don't!" for potential businessmen who show inadequate planning. Fifth, a state-level technical assistance program would be of great value to new businessmen too busy fighting the day-to-day battles to see growth opportunities. Sixth is a strong program to identify local talent, retired or otherwise, to help with small-business problems. A seventh option is organization of more effective local development groups which seek problems of small businesses to be resolved--by someone. And a final option to be considered is the provision of technical training in
high schools and colleges. Wagner concludes with a strong statement for accountability in education and decrying "social promotion" policies which hinder development of productive citizens with skills and strong work habits.

The Determinants of Laws Affecting Small Business

James B. Kau and Paul H. Rubin present an interesting analysis of the determinants of laws affecting small business. They construct a powerful economic argument for leaving safety and health standards (for example) to the marketplace, with employees determining the amount of risk they are willing to take at what wage premium and employers deciding how much investment in safety equipment it might be profitable to make in offsetting this premium. With an extended argument, they demonstrate that OSHA (for example) is economically inefficient and that legislative intervention into the workplace can only be justified on paternalistic grounds. Similar arguments could be marshalled against most government regulation, which, with a requirement of substantial increases in record keeping, have a disproportionate effect on small business.

With this economic background, Kau and Rubin proceed to question why these laws have been passed. In general, groups with concentrated interests will be able to influence legislation even though their gains may be less than the losses of less organized groups. Recently, the problem has been to identify the interest groups.

In a multiple-regression analysis of the voting patterns of congressmen, Kau and Rubin develop some interesting explanations. Ideology, conservative or liberal, was a significant factor in 20 out of the 22 votes studied. Interestingly, the two votes for which ideology was not significant related to appropriations for the Small Business Administration. While conservative voters generally leaned toward positions favorable to small
business, perhaps they opposed government interference in general.

Union contributions were also significant in 20 out of 22 votes, and always had the opposite effect of "Nixon voting," the variable expressing a conservative ideology in a congressional district. Unions generally favor government intervention in the economy. The laws favored by the unions would thus generally hinder small business. Union membership in the congressman's home state was less important, indicating that much of the political power of unions may come from campaign contributions.

Business contributions to congressional campaigns was a significant determinant of votes on seven bills. They were important in explaining two votes on SBA appropriations, two votes on the campaign act, a vote on exempting small oil wells from profit limits, and votes against strengthening the Federal Trade Commission and the Consumer Protection Agency. Strangely, business contributions had no effect on votes regarding OSHA or wage-price controls.

A second analysis of the determinants of campaign contributions shows that unions do a better job of allocating campaign contributions than do businesses. In six out of 10 voting issues, the vote was a significant determinant of union contributions while business contributions appeared influenced by only three out of ten voting results.

6. AVAILABILITY OF CREDIT AND VENTURE CAPITAL

We have included one paper on the capital needs of small businesses in the region. And one paper is enough, for David E. Fyffe has produced an excellent summary of the availability and cost of credit and venture capital for small businesses in the region. To introduce his paper, he reviews the literature on the role of an aggressive financial community in regional development and studies of the feasibility of government intervention in
the capital markets and outlines sources of business financing.

Then, based on questionnaire responses from commercial banks and interviews with other institutions, he examines the availability and cost of credit from commercial banks; the role of SBA in small-business financing with loan guarantees, participation with banks, and direct loans; the effectiveness of Small Business Investment Companies as suppliers of equity capital and long-term loans; the activities of industrial development authorities; and the importance of commercial finance companies as aggressive suppliers of credit.

Similarly, based on responses from a number of recently organized business firms, he looks at the availability and cost of venture capital. Most starts are based on personal assets or investments by close friends and relatives, with venture capital companies interested in the expansion phase for businesses which have survived the hazards of starting. Fyffe looks at the high cost of venture capital and the impact of Federal laws and regulations including the mostly negative effects of the Employee Retirement Security Act of 1974, SEC regulations, and the capital gains tax. He also reviews the perceptions of owners and managers of small businesses regarding the availability of credit.

This lengthy and informative review yields a number of conclusions: Credit is available to small businesses but often at a cost exceeding the rate of return of many young firms. This relatively high cost is simply the result of the cost of funds to lenders, competition for scarce funds, and risk perceptions; there is no evidence of internal imperfections in the financial market. And this relatively high cost is unintentionally, perhaps unavoidably, aggravated by Federal regulatory actions. Paperwork makes SBA loans inaccessible to some small businesses. Venture capital for start-ups is largely unavailable. State and local development agencies are
concerned mostly with promotional efforts and have not explored alternatives for providing small businesses with venture capital.

On the basis of these conclusions, Fyffe makes several recommendations regarding credit and capital: (1) De-couple small business loans at commercial banks from Federal Reserve regulatory actions. (2) Provide tax exemption on the reinvested earnings of small businesses, thus reducing the need for external financing. (3) Increase involvement of industrial development authorities with the starting of new ventures. (4) Simplify SBA loan applications. And (5) examine the role of Small Business Investment Companies to see if they could be made more effective or if SBA support should be discontinued.

7. PROBLEMS, NEEDS, AND OPPORTUNITIES

The final six papers in the volume focus on problems and opportunities, with continued suggestions. We have included papers on the information and research needs of small businesses, opportunities in foreign trade, opportunities caused by shifts in population to nonmetropolitan areas, the problem of rising energy costs, the need for organization planning and management succession, and the favorable influence of an improved transportation network on development of the Southeast.

Information and Research Needs of Small Businesses

Roger H. Hermanson surveys the business information and research needs of small businesses in the region. With responses by 136 out of 400 small businessmen in his sample, he has developed lists of internal information needs, external information needs, and suggested lines of research. In addition, he uses the responses in an analysis of solutions to current economic woes.
The most valuable internal items of information for small businesses are a cash forecast for the coming year, the effects of inflation on average current-asset balances, income after inflationary effects, alternative ways of accomplishing business goals, and costs of complying with government regulations. Hermanson suggests what is only reasonable: that this kind of information can be generated by competent employees or by outside consultants, most likely accountants.

The list of most useful items of external information includes: a summary of financial ratios of similar companies, costs and means of borrowing by similar businesses, a general economic forecast for the coming year, costs and means of obtaining investment capital, and a summary and interpretation of government regulations affecting small business.

Hermanson suggests that the SBA could gather and publish summary financial ratios.

Raising capital is always an important problem and, with an increase in institutional ownership of stocks, could become more serious. Respondents provided ample comments both on their information needs regarding capital and on their financial needs and how to meet them. They include: support of the National Development Council; efforts by the Federal government to ease rigid requirements, cut red tape, and provide adequate publicity; and granting of Federal income tax relief by following the recommendations of the National Chamber's Center for Small Business and of the Small Business Administration itself.

The expression by small businessmen of a need for an economic forecast meant a need for a more accurate one, however derived. On important areas of research, four topics stand out. (1) Ways to reduce government regulation of small business. Hermanson provides an interesting review of
suggestions by his respondents and the high incremental costs of complying with regulations, noting that these costs are the equivalent of a seven-percent increase in the corporate tax rate! (2) Ways to simplify the Federal income-tax law. (3) Ways to reduce the cost of borrowing for small business. And (4) the effect on small business of increasing the minimum wage.

Hermanson concludes his article with a review of the influence of Keynesian economics on government policy; the problem of stagflation, which combines rising prices with unemployment; and a solution to stagflation incorporating the suggestions of small businessmen. These suggestions include: reduce government regulation, simplify Federal income-tax law, find less expensive sources of capital, hold down labor costs through holding down the minimum wage, find means to increase productivity, and find ways to conserve energy. Small businesses in the Southeast are looking for help in establishing an environment in which entrepreneurship can flourish.

Opportunities in Foreign Trade

G. W. Perritt and Arun Prakash explain the status and opportunities of small business in foreign trade. In 1976, only 5.7 percent of manufacturing output of the region entered foreign trade. Only Florida and Mississippi ranked above the national median ranking of states by manufacturing export proportions. And Mississippi's rank of twenty-third is misleadingly high because of a very low total manufacturing output. While the overall growth rate for exports in the region is 15.2 percent and above the national average (14.3 percent) in all but Kentucky and Tennessee, much of this growth rate apparently came from national firms migrating into the region.

Why does the Southeast lag in exports? Perritt and Prakash uncover several reasons. Small businessmen in the region are not motivated, given
the potential profit and associated risks. In addition, they are not prepared by previous education and they have had few of the foreign experiences which stimulate exports. They are bewildered by regulations and lack information on foreign markets.

Further, chance has not turned their way. Of the businessmen surveyed, the decision to export was not part of the strategic plan of the firm. Rather, it was initiated by chance: by an unsolicited order, through a plant visit by a vacationing prospective foreign customer, or through a contact made during a foreign vacation.

Interestingly, Perritt and Prakash find that conferences and seminars attract businessmen who are already involved in foreign trade and do not appear to stimulate exports by new firms. Similarly, the 45 or so banks in the region with international trade departments focus their sales efforts on current, rather than potential, customers. Responses by banks indicate that their role in international trade development is essentially passive. The personnel required to staff trade efforts are not available in any great numbers in the region, few universities offer international business programs, and none offer specializations in international banking.

Perritt and Prakash surveyed universities in the region and found few seriously involved in international business education. They suggest establishing centers for international business education in several universities in the region, sponsored by Federal grants. These centers could form focal points for export development.

Trends in Rural Development

G. Donald Jud explores the role of small business in rural development in the South. This is important because of recent growth trends. Since 1970,
significant population growth has occurred in nonmetropolitan areas. Between 1970 and 1977, a 13 percent increase in population in metropolitan areas in the region has almost been matched by a 10 percent increase in nonmetropolitan areas. In Florida, Kentucky, and Tennessee, the nonmetropolitan growth was substantially above the metropolitan rate. And in Florida, Georgia, Kentucky, and Tennessee, net migration into nonmetropolitan areas exceeded that into metropolitan areas. Only in Mississippi was out-migration from rural areas the case.

Recent studies have shown that this growth in rural counties cannot be explained by adjacency to metropolitan areas. Further, a parallel growth in nonmetropolitan population and employment indicates that people now tend both to live and to work further away from urban areas.

Jud points out that per-capita personal income has risen more in nonmetropolitan areas while cost-of-living differences remain, indicating a significant increase in well-being.

In attempting to understand the factors motivating these changes, Jud observes that all nonagricultural sectors of the economy have recorded employment growth in both urban and rural areas but that the rural growth has been more rapid in every sector except government. Significant shifts occurred in services, trade, finance, and construction, indicating that small towns are severing some of their economic ties with large urban centers. These changes signal new opportunities for small-business development throughout the South.

Jud points out the significant part played by small business in development, noting the findings of David L. Birch regarding the role of small enterprise in the job-creation process. They suggest that much of the employment growth in the rural South has resulted from the birth and
expansion of small, young, independent firms.

Current research suggests that rural development is due to cost factors and to a heightened desire of individuals, managers, and entrepreneurs for the natural amenities of outlying areas. Planners need to be aware of the diverse growth patterns of these areas. And since recent research raises doubt concerning the effectiveness of regional growth promotion plans aimed at large corporations, Jud suggests that stronger attention be directed toward small business in nonmetropolitan areas. An assistance program based on the county extension agent network of the Department of Agriculture may be the answer.

Rising Energy Costs

William D. Donnelly writes about the effects of the "energy crisis" on small business in the region. In a review of energy developments in recent decades, he identifies three factors which have led to our current energy problems. First, the industrial revolution and relatively cheap energy led to an extensive reliance on energy-using equipment and processes. Relief on this point will come in the long run as the existing stock of capital is replaced with energy-efficient equipment. Second, the relative price of energy has, and is, changing rapidly due to the politics of the Middle East and a rising tide of nationalism. Price increases and reductions in supply should be anticipated. And third, multinational oil companies should be expected to maximize profits and thus to reinforce OPEC's actions.

Donnelly finds that energy consumption per dollar of value added by industries in the region is greater than the national average. This may be due to a number of factors, including the energy-intensity of the production process, lower wages, etc. In spite of this, he expects rising energy costs
to reinforce the effect of lower labor and site costs in increasing the shift of economic activity from the Midwest and Northeast to the Sun Belt and the West.

Donnelly speculates on the effect of rising energy costs on small business in the future. He stresses an increased emphasis on energy conservation in short-run energy management and in long-run redesign of buildings and equipment. In the region, solar energy devices may increase and we will see a shift from large-scale energy production to smaller facilities and co-generation of power with use of now-wasted heat.

With revitalization of central cities to reduce energy waste, he anticipates a reversal of the trend toward increasing urban sprawl over the next two decades. He suggests that the current wide dispersal of retail outlets cannot be sustained under conditions of high energy costs and that drive-in restaurants and facilities catering to automobile travelers will be hard-hit. Trends fostered by modern highways will not continue. Individuals will respond with movements away from increasingly dispersed suburbs and toward higher-density living. Small business must be ready to adapt to these changes.

**Organization Planning and Management Succession**

Curtis E. Tate recounts a series of cases taken from his experiences with small business in the Southeast and emphasizes the importance of organization planning and management succession. Organization planning has a number of purposes, including: to provide for division and specialization of labor; to provide for direction and control; to make possible an effective organizational structure; to provide an awareness of organizational needs; to provide order; to define roles, relationships, communication channels, and
responsibility; and to provide management continuity. Tate explains each one of these anecdotally and then, with a series of mini-cases, illustrates the problems which arise in small businesses which ignore the planning process.

Management succession is obviously a major problem in small business. Tate enumerates the purposes of planning management succession: to provide for growth, expansion, and acquisition; and to provide for such management contingencies as illness, injury, retirement, and death. The problems to be overcome include family emotions, the one-person-show problem, unwillingness to confront the uncertainty of life's contingencies, status-quoism, personal greed and selfishness, and a belief that life on earth is eternal. Tate's mini-cases to illustrate these points are again enlightening.

**Transportation Networks**

Finally, the volume ends on a happy note.

Joseph L. Frye and Frank L. Hendrix have produced a summary review of modes of transportation in the region and find that the region is blessed with one of the finest and least expensive transportation networks in the nation, an obvious advantage to all business firms in the region.
THE ECONOMIC HISTORY OF SMALL BUSINESS IN THE REGION

Jack Blicksilver
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1. OVERVIEW

In many respects the economic evolution of small business in SBA Region #4 has paralleled trends affecting small scale enterprise throughout the nation. The pace and performance of the national economy, the stage in the business cycle, the legal environment and government fiscal and monetary policy have created a common framework for enterprises of different sizes in various regions of the nation. In significant respects, however, the history of business enterprise, and particularly small business, in the region has been unique, shaped over a 300-year time span by a spate of localized physiographic, demographic and socioeconomic forces.

Business enterprise in the region from its very beginning was linked inextricably to world economic trends. The mercantilistic policy pursued by the mother country, combined with a warm climate, long growing season and extensive timber resources, placed an early emphasis upon the production of primary products, food and fibers, for ultimate consumption by more mature, industrialized economies. During its century long colonial experience and throughout much of the 19th century, the region exemplified the Jeffersonian ideal of a largely rural, agrarian economy, with commerce serving as the handmaiden of agriculture. Moreover, in the more western parts of the region, the frontier experience persisted for a half century after political independence was acquired, cheap land luring the ambitious and the discontented. A third molding force, which counteracted to some degree the democratizing impact of the frontier, was the region's long reliance upon a dependent labor supply, initially white indentured servants and later black slaves. For almost
two-thirds of the region's historic evolution its limited capital was channeled almost exclusively into acquiring a larger labor force and additional land for it to cultivate. For many decades after their emancipation, freedmen and women, geographically mobile and equipped with a range of skills acquired under slavery, were provided little encouragement to contribute significantly to the growth of the region, either as consumers or as entrepreneurs.

The prevalence of large numbers of black and white farm-reared workers supplied the initial stimulus to post-Civil War industrialization. The range of manufacturing industries which spearheaded the region's take-off to economic growth was narrow, bunched around a small core of industries concentrating on the local processing of raw materials and agricultural commodities. Although native capital and entrepreneurship spearheaded the "cotton mill crusade," largely in terms of small business enterprises, the region's labor surplus and slower overall growth rate discouraged a mass influx of foreigners whose range of skills and broader consumption patterns fueled rapid expansion in other sections of the nation.

Only during the past three decades have confining links with an economically stagnant past been severed sufficiently for the region to move forcefully into the mainstream of American economic life. In the process, all segments of the population--white, black and a range of newly arrived immigrant groups--have played important roles. The region's broadened economic base and accelerated rate of growth has been characterized by an increasing number of small business enterprises as well as by the growing prominence of median-and large-scale native enterprises which were initiated as small businesses. More so than most other regions, the current economic status of SBA region #4 and the role of small business within the region are the product of historic forces at work since the mid-17th century.
2. HISTORIC ROOTS OF SMALL BUSINESS IN THE REGION, 1660-1776

The South was the nation's first section to develop capitalistic agriculture. Staple crop production was initiated in Virginia by the joint stock commercial enterprise which founded the colony; those engaged in extractive pursuits in the other southern colonies were made more sensitive to world market trends than were the more self-sufficient farmers in the non-South. The section's economy as it evolved during a long colonial era was dominated by agribusiness and by closely linked commercial services.

Settlers to SBA region #4, migrating to the New World a half century after Virginia was founded, adopted and in some measure reshaped many of the practices found successful in the pioneer colonies only after costly experimentation. The region's economy, as it then evolved over the span of a century, was further molded by the interaction of three additional powerful forces: (a) an extensive inflow of Europeans from a diverse group of nations, supplemented by considerable migration from the northern colonies; (b) a trend toward larger scale farming operations which placed a premium upon a reliable labor supply, a need met first by indentured servants and after the 1680's, increasingly by a slave labor supply; (c) easy access to cheap land, made possible by an expanding geographic frontier, which was not closed in the region until the 1840's.

The headright system, initiated in Virginia, became widely adopted as the most feasible means of attracting settlers to a colony. Under this system, a parcel of land was given to any immigrant who financed his own passage to the colony; an additional unit was provided the head of household for each person he brought with him. For those unable to defray the cost of passage, the system of indentured servitude was soon devised. Under this system the cost of passage of an impoverished immigrant was met either by a sea captain transporting settlers to the New World or by a colonial businessman requiring additional
labor. The person seeking transportation signed a contract committing his labor, typically for a period of from three to seven years, in return for the price of his passage. At the close of his period of indenture, the person was legally liberated and often was also granted a parcel of land. In an undeveloped area, with seemingly inexhaustible quantities of land and a paucity of people, the headright and indentured servant systems utilized abundant and low priced resources to underwrite settlement. For thousands of European peasant farmers, forced off the land by enclosures or harried out of their home country by religious or political persecution, indentured servitude was a necessary stage in the process of becoming an independent farmer. For non-English speaking immigrants, of which the Germans were numerically the most important, the indenture contract also enabled the newcomer to acquire a knowledge of the prevailing language and dominant institutions.

Throughout the settled parts of the region during the first half of the 18th century, extensive numbers of farmers of humble origin climbed upward into the middle and some even into the large planter class. A planter aristocracy, characterized in the early decades of the 18th century by large land holdings, staple crop production for the foreign market, and an ownership of slaves numbering twenty or more, emerged in South Carolina and became more rigid as the period progressed. Nonetheless, as L. C. Gray in his authoritative History of Agriculture in the Southern United States to 1860 concludes: "Indentured servants, pioneer farmers, and merchants succeeded in climbing into the charmed circle."

One of the salient characteristics of the period after 1700 was the steady replacement of white European indentured servants by black African slaves. South Carolina had fewer than 2,500 black persons in 1700; by 1720 the colony contained 12,000 blacks, and by 1740 the number reached 30,000.
The significant shift in labor supply, which had profound repercussions upon the economic and social development of the region, was caused by a variety of factors. Some indentured servants proved to be unreliable and truculent; the short time span of the typical contract made it necessary to periodically recruit and train a fresh labor supply. For farmers seeking a competent, reliable labor force, whose average cost over time could be expected to be lower than that for a succession of indentured servants, slaves were increasingly regarded as the superior investment. In North Carolina, with a slower and more limited development of staple crop production, indentured servants were never numerous. The number of blacks in the colony increased from 415 in 1700 to 11,000 by 1740. By the time Georgia was founded in the early 1730's slavery had become firmly entrenched in the region.

Paralleling the shift from indentured servitude to slavery in the settled, more intensively cultivated parts of the region was the penetration by newcomers and indentured servants who completed their contracts into the heavily forested frontier areas. During the latter decades of the 17th century, a flow of immigrants arrived in South Carolina to establish their homes as small freeholders. Some had been artisans or yeoman farmers in England; considerable numbers moved southward from Virginia, New York and even the New England colonies. Small scale farmers also arrived from the West Indies where they were being squeezed out by large scale sugar planters. As a result, eastern South Carolina emerged from frontier conditions as an area dominated by a diversified economy.

Relatively small plantations evolved, with rice as the principal staple. On the further edge of the frontier, pioneer farmers relied principally upon Indian trading, herding of cattle, and activities related to lumbering, particularly the making of barrel staves, shingles, clapboards and the processing of pitch, tar and turpentine.
The major exception to the largely English composition of the region's white settlers in the 17th century was an influx of upwards of 500 French and Swiss Huguenots. The initial group arrived in 1680, but the prime surge of settlers arrived following the revocation of the Edict of Nantes in 1685. The largest settlement outside of Charleston took place on the Santee River, 60 miles to the north. Two settlements were established under Swiss leadership, one at Purrysburg, South Carolina and one at New Bern, North Carolina. Most arrived without property, although in Europe they had been solid members of the middle class, as farmers, artisans and merchants. A few had migrated with sufficient means to purchase land, but the majority secured title under the headright system. Welcomed to the English New World in the hope that they would establish the silk and wine industries, the hard working, entrepreneurially-minded Huguenots failed in that regard, but did succeed in overcoming great obstacles to carve out highly successful careers as merchants, planters and manufacturers, as case studies of the brothers Pierre and Gabriel Manigault and the Laurens family, father and son, reveal. The stories of their lives, as well as those of the women in their family, such as Judith Giton Manigault, illuminate the process by which small scale business endeavors could eventually lead to large scale activities, as early as the first quarter of the 18th century.

Few ethnic groups migrating to the region had as great success in so short a time span as did the Huguenots in the Carolinas. But, the magnitude of their success, as well as forces operating both within the region and on the European continent, led to a considerable direct influx of non-English people. In the early 18th century, South Carolina's active immigration policy attracted groups of Swiss and German Lutherans who established settlements on branches of the Pedee and Santee. There were two distinct waves of Scotch immigration, 1745 to 1755 and 1760 to 1770, following the unfortunate uprising of 1745 and the
disintegration of the clan system. North Carolina shared significantly in the homesteading of this sturdy group.

The settlement of North Carolina was confined largely to the coastal plain until the 1730's, when a southward migration began from the middle colonies along both sides of the Blue Ridge. The settlers were largely recent immigrants from Scotland and Germany. The Scottish settlers tended to scatter; the Germans settled in compact communities. Both groups largely avoided slaves and carried on diversified farming with an emphasis upon small grain, abundant orchards, and the raising of flax and hemp. Their surplus production of wheat and tobacco was hauled laboriously to fairly distant markets.

Further to the southwest, Georgia's original colonization plan called for small landholdings, exclusion of slavery and safeguards against land engrossment. The plan did not materialize and after 1750 the low country rapidly became a region of rice and indigo plantations, as well as timber and naval stores production. The up-country, however, evolved in a manner similar to that of South Carolina. It was occupied first by Indian traders and cattle herdsmen, followed by a wave of small farmers who moved down the Appalachian valleys and developed a largely self-sufficing economy, supplemented by hemp, tobacco and livestock as cash commodities. After 1763 the land area available for settlement was greatly enlarged by Indian cessions. The treaty concluded with Spain that year opened for settlement an additional one million acres in southwest Georgia. It also opened Florida for the first time to English settlement and for the next two decades colonial businessmen trafficked in lumber and deer skins in west Florida but did little to develop the orchards and citrus fruit production started by the Spanish in east Florida.

Despite British attempts to confine colonial settlements west of the Allegheny Mountain chain, penetration into the lands beyond took place by
mid-18th century. The first southerners to cross the mountain barrier were Scotch-Irish and German redemptioners who had occupied the piedmont of North Carolina. The first log dwelling was constructed in Kentucky in 1748, and a few small settlements were established prior to the adoption of the Declaration of Independence. The pioneer settlements in Kentucky screened Tennessee from Indian attacks from the north and provided favorable conditions for communities established in the valley of east Tennessee. The site of Nashville was first visited in 1761. Meanwhile, considerable migration into the Natchez country on the east bank of Mississippi began in the mid-1760's. The initial settlers, from Georgia and the Carolinas, included a number of substantial farmers and planters as well as rude frontiersmen.

By the beginning of the struggle for political independence some settlement had taken place in all parts of the territory that was to eventually become the 8-state SBA region #4. The three original states (South Carolina, North Carolina and Georgia) and the two territories (Kentucky and Tennessee) which were included in the nation's first census in 1790 had a more heterogeneous population than the new nation as a whole. Throughout the region there were large numbers of Scotch, Irish (from Ulster and Free State), German, and French ethnic groups. The initial contingent of French Huguenots was supplemented in 1755 when about 1,500 Acadian refugees arrived in Charleston. Jews, primarily from Spain, resided in the South since the 17th century. The 1790 census disclosed that about half of the 1,500 Jews in the nation lived below the Mason-Dixon line. Charleston, with 200 Jews in 1790, had the second largest Jewish population in the new nation.

The region was later to become increasingly homogeneous, as succeeding waves of immigrants bypassed the South until the mid-20th century. For a century and a half following the formation of the new nation, the region failed
to benefit from the inflow of newcomers with capital and initiative to contribute. Nonetheless, by 1790 the region's melting pot, already containing an abundant mixture of western European ethnic groups, was set to simmer slowly.

During the long colonial era, numerous members of the region's varied ethnic groups resided in seaport towns or in the smaller interior communities, serving as intermediaries in the growing flow of rice, indigo, hemp, naval stores, livestock and processed timber being shipped to England, the West Indies and New England in exchange for tools, hardware, dry goods, sugar, spices, and a wide range of luxury products for the more affluent settlers. The vast majority of commodities in foreign trade flowed through the port of Charleston, which, with a population of 11,000 in 1770, was the commercial capital of the South.

Much of Charleston's international trade was handled by resident factors, largely English or Scottish, serving as representatives of British firms. In addition to dominating trans-Atlantic shipping and the domestic wholesale trade, factors largely directed the importation of indentured servants and slaves. After 1732 Savannah vied for the trade with the interior, but its much smaller mercantile community found it difficult to compete effectively with the larger stock and more extensive credit made available by Charleston's factors and commission merchants. Whereas Charleston and Savannah concentrated on commercial relations between the colonies and the home country, a number of minor seaports--Port Royal, Georgetown, Edenton, Sunbury--dispatched smaller vessels to conduct trade with the West Indies and carry on coastwise commerce with colonies to the north.

Physical geography played a part in determining the scope of the seaboard merchants' trade with the back country. Although Charleston's harbor was excellent, the shoal channels of the inland streams thwarted attempts of ocean
going ships to penetrate into the interior. Smaller vessels were required and the way was prepared for smaller businessmen.

As the interior of the Carolinas and Georgia was settled, back country communities became linked with the port cities by either inland navigation or by wagon roads. Crossroads general stores soon followed the successful cultivation of the surrounding countryside. Some stores were branches of the larger seaboard-based firms; others were locally owned and operated, sometimes in conjunction with other employment. Typically, interior storekeepers supplied local farmers and planters with hardware and groceries, sometimes with additional slaves, both on credit and through barter arrangements, while at the same time handling the surplus commodities of the adjacent area, often on a commission basis for a larger seaboard merchant.

Whereas the magnitude of business generated by a representative regional up-country settlement during the 18th century was insufficient to support more than a single general mercantile enterprise, the seaports were able to accommodate a wider range of specialized small business firms. The hundreds of ships which cleared Charleston's harbor annually supported ship builders and repairers, keepers of ropewalks as well as numerous other enterprises involved in outfitting vessels and providing for the varied wants of seamen while on shore. Other small businessmen whose roles as skilled craftsmen typified a dynamic port community during the colonial era included coopers, carpenters, bricklayers, silversmiths, cabinetmakers, brass founders, painters, shoemakers and tailors. Due to the relative thinness of the market, those engaged in handicraft work often conducted small retail shops in conjunction with their specialized craft. Thus, Huguenot immigrant John Laurens began his business career as a saddler, gradually expanding his scope of enterprise to become eventually one of the largest merchants in the province.
Upward mobility was a distinct possibility for able tradesmen in the 18th century and case studies could be limned of hatters, carpenters, and shipwrights joining South Carolina's elite. As the demand for their goods or services grew, small businessmen took on apprentices and some purchased slaves. Indeed, on the eve of independence, half the population of Charleston was black. Since slaves were priced in proportion to their ability to perform highly valued jobs, plantation slaves in large numbers were taught specialized crafts and were hired out, providing their owners with returns of 15 to 20 percent on the initial investment. It seems evident that the widespread reliance upon black slaves as mechanics and craftsmen on plantations and in the cities discouraged the development of the mechanics arts among whites. Their general unavailability in the region was in part compensated in the ante-bellum era by an expanding number of free black artisans and small businessmen.

In a region characterized by a high mortality rate as well as by a paucity of skilled white male artisans and supervisors, white women from early colonial times contributed importantly to business activity, particularly in the service sector. In 18th century Charleston, women operated boarding houses and dame schools, conducted dancing classes and kept stables in connection with lodging houses. One notable businesswoman, Ann Timothy, continued to publish her husband's newspaper after his death and in 1783 was appointed printer to the state of South Carolina.

More significant, although less publicized, were the numbers of women who managed plantations, large and small. Supervising a labor force in household production and often in field work, southern women seized the opportunity to exercise management skills which often resulted in profitable business enterprises. A few can be credited with major innovations. In the early 1740's, Eliza Lucas found herself in charge of a South Carolina plantation. An avid
amateur botanist, Ms. Lucas began to experiment with a variety of seeds, including indigo, which she planted and after much effort succeeded in devising an effective formula to extract the dye. By 1747, Charleston began exporting large quantities of indigo which the Lucas and neighboring plantations grew. Although most indigo was produced on large plantations, where it became a major money crop, some was cultivated in the back country by small South Carolina and Georgia farmers who produced a fine grade through careful attention to the tedious process of extracting the highly prized vegetable dye.

3. THE EXPANDING AGRICULTURAL-COMMERCIAL ECONOMY, 1776-1860

The structure, pace and essential character of the regional economy underwent little change during the decades following political independence. The evolving frontier and the plantation method of farming continued to be the dominant influences shaping the regional economy. As late as 1830, Alabama, Mississippi and western Tennessee were within the frontier line. Along with the removal of the remnants of medieval restrictions and the protection to private property accorded by the Constitution, the constantly expanding frontier--across the Blue Ridge mountain chain into Kentucky and eastern Tennessee, southwestward into the rich black belt of Alabama and Mississippi, and the opening of Florida following its purchase from Spain in 1819--provided the greatest stimulus to small business activity.

For a short time at the close of the Revolutionary conflict, the plantation system seemed destined to displacement, with rice and tobacco suffering from declining productivity and indigo no longer a viable crop. By the early 1790's, however, cotton cultivation began to replace the colonial staples as the region's major cash commodity. Its success was assured by the soaring demand of British textile manufacturers and by the introduction of Whitney's cotton gin. Slavery, seemingly moribund, rapidly revived. In the region's
initial cotton belt, the piedmont of South Carolina and Georgia, the labor-intensive plantation system peaked and then began to decline in importance as a southwestward migration to more level and fertile lands accelerated. A painful adjustment to more diversified agriculture began.

In the booming territory being opened to new settlement business enterprise flourished. Attorney-author Joseph G. Baldwin, residing from 1836 to 1853 first at Dekalb, Mississippi and then at Gainesville, Alabama, wrote a series of sketches, The Flush Times of Alabama and Mississippi, which depict facets of the dynamic frontier environment as planters, sharp traders and shrewd attorneys vied for prestige and profits.

Throughout the region, despite aggressive efforts to recruit white workers and stimulate industry, agriculture continued to predominate and the region remained more rural than did the non-South. Whereas, on the eve of civil war, one of every five persons in the nation resided in a community of 2,500 or more, Alabama's population was only 5.1 percent urban; Georgia's 7.1 percent; South Carolina's 6.9 percent; and Mississippi's 2.6 percent. Of the region's largest urban centers in 1860, Mobile, with 29,258 persons, had 3 percent of Alabama's population; Savannah, with 22,292 persons, had 2 percent of Georgia's population; Natchez, with 6,617 had 0.8 percent of Mississippi's population; Charleston with 40,522 had 6 percent of South Carolina's population; and Memphis, prosperous Mississippi river port, had only 22,623 residents, barely 2 percent of Tennessee's population.

Although large, efficiently managed, slave operated plantations succeeded in capturing control of the region's most fertile land, small scale commercial farming remained profitable. Georgia illustrates the emerging process of geographic specialization. As the state's best remaining soil for cotton cultivation was being acquired by aggressive planters in the 1840's, smaller
farmers retreated to the valleys and coves of north Georgia. Those who persisted in staple crop production adjusted to falling farm prices by practicing greater efficiency and by diversifying crops produced for market sale. Small farmers in the state spearheaded the movement toward agricultural reform; in middle Georgia, they began to plant orchards, especially peach trees. Some also began to mine clay and marble.

North Carolina and the newer states, Kentucky and Tennessee, became major producers of tobacco. The crop was grown best on family operated farms or on small plantations with a limited number of closely supervised slaves. By 1860 Kentucky and Tennessee were second only to Virginia as producers of tobacco, with North Carolina in fifth place.

Even in the heart of the region's cotton production, Alabama's black belt, land ownership in mid-19th century was widely diffused. The largest group of slaveholders owned only from 100 to 200 acres of land and a majority of slaveholders owned only a few slaves and worked in the field with them. In the Alabama piedmont and pine barrens, the large planter class was virtually non-existent, while in the black belt it amounted to only 12 percent of the entire slaveholding group.

In the commercial sector of the region's ante-bellum economy, the factorage system retained its dominant position and, on balance, retarded the development of interior towns and up-country storekeepers. It did so by concentrating capital and credit in the larger coastal cities and river ports. These centers, able to dominate the peripheral trade area, limited the growth of smaller communities and circumscribed the range of their socioeconomic functions. Medical and legal services were concentrated in the larger mercantile centers as were purveyors of such recreational and cultural services as bookshops and theatrical companies.
In the region's general crop areas a limited number of towns emerged, in which the salient economic force was the storekeeper. Typically, country merchants, as in the colonial era, provided credit from one planting season to another, and often assisted farm customers in disposing of surplus commodities, thus paying off accumulated bills. The ante-bellum storekeeper differed from his colonial counterpart in acquiring his stock of merchandise from large northeastern wholesalers from whom more liberal credit could be obtained than from southern seaboard merchants. In an increasingly monetized economy, the 19th century storekeeper was often required, in the absence of adequate banking facilities, to perform a range of financial functions, including accepting deposits and paying bills for farm customers. When banks were established in small southern towns they lessened the demand on country storekeepers, but seldom did they provide a full range of adequately performed financial services.

Portions of the region which lacked sufficient purchasing power to sustain local stores were served by peddlers who functioned somewhat like circuit riding preachers. Working out of the larger interior cities, peddlers sold on a farm house to farm house basis a wide range of dry goods, patent medicines and trinkets. In lieu of cash they accepted in payment sassafras, skins, eggs and chickens which in turn they wholesaled. First generation immigrants often relied on peddling to accumulate sufficient capital to open a small crossroads store.

Atherton's The Southern Country Store, 1800-1860 concludes that operating a country store in the ante-bellum period was a prestigious and often a profitable enterprise. Risks were high due to sharp price fluctuations on goods in inventory and products taken in trade. The potential for large inventory losses was reduced somewhat after the panic of 1837 by the passage
of limited liability legislation, which made partners responsible only for the
amount invested in the enterprise. The states of Alabama, Florida, Georgia,
South Carolina and Tennessee adopted such legislation. In fact, the rate of
mercantile bankruptcies was higher in the region than in the non-South. Business
failure was not, however, associated with moral delinquency. Atherton concludes
that "the South wanted merchants and respected the occupation."

As the economy of the region expanded, a shift took place in the direction
of mercantile specialization. Up-country storekeepers, when faced with the
decision, typically concentrated on groceries, dry goods or clothing depending
upon past receipts and the estimated potential of each line of goods. The
population of the town and the size of its hinterland trading center largely
determined the number of specialized shops it could support. In the mid-1850's,
Clinton, Alabama with a population of 250 contained four dry-goods stores, one
grocery and one drug store; Eutaw, eight miles away, the county seat, with
1,200 residents, contained four dry-goods stores, one clothing store, three
drug stores, one confectionary, several grocery stores and one book store.

The region's low per capita income as well as the extensive reliance upon
household manufacturing discouraged the development of the factory system.
Production of goods by members of the family for home consumption reached its
peak in the more settled parts of the region prior to 1815. The value of
household manufacturers in 1810 has been estimated at $2.1 million for Georgia
and $3.0 million for North Carolina; for the newer states of Tennessee and
Kentucky the estimated value of household production was $1.7 million and
$2.4 million respectively. The surge of manufacturing activity in the non-South,
particularly during the 1840's, left the region far behind. The pace of
regional manufacturing activity picked up somewhat during the 1950's; its
structure was dominated by small, locally financed establishments processing
locally produced agricultural commodities, primarily for a regional market.
By 1860, cotton goods emerged as the region's major manufacturing industry. E. M. Lander's careful study of The Textile Industry in Antebellum South Carolina illuminates the main impediments to greater growth. The larger mills of the lower counties were able to tap the mercantile capital of Charleston, but they suffered from an unreliable source of power. They utilized slave labor with considerable effectiveness, but found this source scarce and costly in the 1850's when slave and cotton prices soared. Piedmont plants benefited from skilled supervisors, often imported from the north, and sufficient motive power. But the white work force drawn from rural communities, while plentiful, lacked discipline. Many mills were undercapitalized and inaccessible. For the South as a whole the 300,000 spindles housed in 159 establishments led to a value of cotton textile output in 1860 only one-tenth that of New England. Landers conclusion for South Carolina mills--that most "were financially insecure and economically insignificant,"--could be applied to the industry throughout the region.

Textile production was supplemented in the ante-bellum period by factory output of boots and brogans, mostly for rough farm use, simple carriages, wagons and carts, some men's clothing and tobacco. Tobacco processing, concentrated in North Carolina, was a small scale operation, with the average plant employing fewer than 50 workers. Most tobacco factories were located in small towns. By 1857 there were three in Yanceyville and five in Milton. Durham's first tobacco factory was established in 1858. The entire state in 1860 produced $1.1 million of tobacco while employing 1,641 workers.

Although manufacturing had a limited impact upon the region's overall economy, it provided an entrepreneurial outlet for local businessmen and brought a number of able managers and skilled technicians to the South. A sizeable segment of this professional business group staked their lives and
fortunes to the region during the Civil War and post-bellum era. Pre-war manufacturing activity also demonstrated that black as well as white workers, if properly supervised, could be highly efficient.

In 1860 the region's leading manufacturing states in terms of capital investment were South Carolina ($24.3 million) and Kentucky ($20.3 million). These were also the states with the highest annual value of products and the largest number of employees (South Carolina, 32,500 and Kentucky, 21,300). North Carolina had the most manufacturing establishments (3,689), followed by Kentucky (3,450). Only in South Carolina did women constitute more than one-third of the manufacturing labor force.

With limited opportunities for employment in manufacturing or in gaining access to good, cheap land, the region had limited appeal for the large numbers of Irish, Scandinavians and Germans who migrated to the United States in the 1840's and 1850's. The region became far more homogeneous in population than it was during the colonial period; in 1860, the percentage of foreign born to the total population ranged from a high of 2.4 percent in Florida to only 0.3 percent in North Carolina. Nonetheless, a sizeable number of newcomers viewed the region as an attractive area in which to launch a business. Their numbers were swelled by northerners, often associated with mercantile firms in major trade centers, who migrated south. Attracted to small and medium sized communities, the transplanted Yankees typically retained close personal and business ties with their states of departure while establishing firm, and often permanent, commercial and family roots in their adopted region.

A study of Natchez, based on unpublished 1850 census returns, disclosed that more than half the residents have been born outside of Mississippi and more than one-third were of foreign birth. More Yankees were present in the city than were non-Mississippi southerners.
Settling initially in cross-roads communities, "greenhorns" with negligible capital and a limited English vocabulary viewed the South as a land of upward mobility. Particularly was this true of German Jews. By 1860, perhaps a fourth of the 150,000 Jews in the United States resided in the slave states. Southern towns with Jewish congregations in 1860 included Mobile and Montgomery, Alabama; Augusta, Columbus and Macon, Georgia; Louisville, Kentucky; Jackson, Port Gibson, Vicksburg and Natchez, Mississippi; Charleston and Columbia, South Carolina; Knoxville, Memphis and Nashville, Tennessee. At least nine additional towns, including Atlanta, had Jewish cemeteries or benevolent associations. Moreover, countless numbers of Jewish storekeepers were based in hundreds of smaller regional communities and as peddlers Jewish businessmen brought a range of consumer goods to scattered farm families throughout the region.

Equally important was the emergence in the ante-bellum era of a core of free black businessmen. The total number of free blacks in the region was small. It ranged in 1860 from as few as 773 in Mississippi (0.2 percent of the population) to 30,463 in North Carolina (8.4 percent of the population). On the eve of the Civil War there were approximately 66,000 free blacks in the region. In addition, numbers of free blacks moved north when the southern socio-political environment became increasingly hostile, particularly in the 1850's.

A number of free blacks managed to acquire land in the region. Most of them engaged in general farming, although some became small planters and a very few acquired slaves. Approximately ten percent of North Carolina's free black population was listed as owners of property in 1860. Of this group, about a third (1,211 persons) owned real estate valued at just under a half million dollars.
In the urban South, free blacks possessing skills as craftsmen rose in notable instances to the status of small businessman. Following the slave insurrections of the 1830's, several states in the region passed legislation which prohibited the use of slaves in businesses in which knowledge of reading or writing was required. This restriction slowed the process by which slaves could accumulate the wealth necessary to purchase their freedom. Although the relative importance of free blacks in the urban South waned after 1840, their position often challenged by newly arrived immigrants, they remained dominant in occupational categories in which a premium was placed upon physical labor and competent personal services. In cities throughout the region free blacks were mechanics, coopers, cabinetmakers, cordwainers, both in repairing and making boots, bookbinders, cigarmakers and tailors. They served as draymen and haulers of freight. They were especially active as barbers, butchers and in the livery business. Free blacks, with an excellent reputation for cooking, ran several cafes and a number of fine quality restaurants.

Charleston in 1860 had about 700 employed free black males, including 122 carpenters, 87 tailors, 30 shoemakers, and 23 butchers. Not all were self-employed, of course, but there were 371 free "persons of color" who paid taxes on real estate valued at about $1 million. In the region's major port city, blacks were active in owning and operating boats; one free black boat builder employed both black and white labor. There were several free black fishermen and one black family enterprise was represented by the sign: "Joe Cole and Wife--Fish."

Business opportunities were enhanced for free blacks by the fact that the core of their clientele, as barbers, cooks, draymen and craftsmen, were white southerners. When the movement for racial segregation mounted, some free blacks managed to remain unmolested. In Alabama, a black contractor and bridge builder
was so highly regarded that the legislature of the state passed a special enactment allowing him to pursue his business. The business career of Lunsford Lane in Raleigh, North Carolina, illustrates an opposing and more common course of action. After purchasing his freedom with the profits from the production and sale of a superior smoking tobacco, Lane opened a general merchandise store and wood yard and eventually purchased freedom for his wife and six children. The antagonism of lower class whites grew too strong, and Lane was eventually pressured into leaving the state and region.

Very few of the business enterprises developed by free blacks survived the civil conflict. Acquired skills could be passed down to a younger generation and the ideal of business independence did, however, reassert itself among emancipated blacks in the post-war era.

3. CIVIL CONFLICT AND THE SLOW PROCESS OF RECOVERY, 1860-1940

The economic cost of the Civil War and the causes of the prolonged regional recovery have been enduring subjects for scholarly speculation. Much less debatable is the observation that the region remained until World War II primarily rural and agricultural, and if anything more narrowly involved in extractive, primary production for external markets and more heavily dependent upon outside financing of its large scale enterprises.

Among the adverse regional effects of the civil conflict, as assessed by authors Goldin and Lewis, were large capital losses, extended socio-political instability and widespread commercial disruption. As late as 1909, southerners on the average consumed about 30 percent less than they would have consumed had pre-war per capita consumption levels been sustained.

Union victory resulted in the liberation of 2.6 million slaves residing in the region. A mobile labor force was created as well as a large pool of potential small business entrepreneurs. The most significant immediate impact,
however, was the inevitable disruption of ante-bellum standards of forced labor and supervised discipline. A sharp decline in the black labor force participation rate took place, as considerable numbers of black women ceased working and black males exhibited a preference for a shorter work day and additional leisure, even if it meant a somewhat lower standard of living. A recent study by Random and Sutch, *One Kind of Freedom*, concludes that following emancipation the total male equivalent work hours supplied to agriculture on a per capita basis declined by about one-third. Supplementing the decline in work effort and the loss of economies secured by large scale plantation production as major factors in the region's abortive recovery effort was the declining position of southern staples in the world economy. There began in the late 1860's a three decade-long slide in world prices of major agricultural commodities.

During the entire period 1865 to 1940 the region remained far more rural and agricultural than the nation. In 1900, two of every five Americans resided in an urban setting; Mississippi and North Carolina were more than nine-tenths rural, and the region's most urbanized states, Florida and Kentucky, had 20.3 percent and 21.8 percent of their population respectively living in cities of more than 2,500 persons. The region's urban lag continued through the depression decade. In 1940, 56.5 percent of the nation's population lived in cities; in the region, except for Florida's 55.1 percent urban dwellers, the range extended from 19.8 percent in Mississippi and 24.5 percent in South Carolina to 34.4 percent in Georgia and 35.2 percent in Tennessee.

The region's rural population, primarily engaged in agricultural pursuits, was afflicted with underemployment and low productivity. In 1890 the percentage of the labor force engaged in farming stood at 34.6 percent in Alabama, 39.7 percent in Mississippi, and 40.6 percent in South Carolina. In very few non-southern states was agricultural employment so predominant. The value of
agricultural output per worker was far lower in the region than the national average. In 1890, it ranged from $136 per agricultural worker in North Carolina and $168 in Tennessee to $202 in Georgia and $205 in Mississippi. By comparison the value of farm output per worker in Maryland was $292, in Michigan $306, in Pennsylvania $385, in Illinois $431. The combination of rural overpopulation and low agricultural productivity were major manifestations of regional backwardness in the post-Civil War decades.

Viewing post-bellum census data which enumerated the expanding number of southern farm units, contemporary observers drew a false conclusion. Poet Sidney Lanier proclaimed the emergence of the sturdy, self-sufficient, southern farmer, producing "meat and bread for which there are no notes in banks, pigs fed with home-made corn . . . eggs, chickens . . . products of natural animal growth, and grass at nothing a ton." In quoting Lanier, historian C. Vann Woodward in his authoritative Origins of the New South commented: "It was an inspired vision, and it represented everything that the southern farmer was not and had not."

Much more characteristic of regional agriculture than the diversified family owned farm was the tenant operated unit producing a single staple, typically cotton, often under a share cropping arrangement. The regional trend toward greater agricultural specialization can be illustrated by Georgia. Between 1881 and 1900 Georgia's production of cotton increased from 814,000 to 1,200,000 bales and its output of corn from 23 to 34 million bushels. During the same time period, the state suffered a steady decline in the amount of small grains, hay and oats cultivated and in the number of beef cattle, dairy cows, sheep and most fowl. Production of wheat declined over 1.2 million bushels, causing four of Atlanta's five flour mills to close because of insufficient grain for commercial milling.
The pattern of increased regional specialization persisted through the first third of the twentieth century. In 1938, the United States Government's Committee on the Conditions of the South, as cited by Clark in *Three Paths to the Modern South*, concluded:

The farming South depends on cotton and tobacco for two-thirds of its cash income. More than half its farmers depend on cotton alone. They are one-crop farmers. ... All their eggs are in one basket, which can be upset, and often is, by the weather, the boll weevil, or the cotton market.

By the 1930's well over half the region's farmers were tenants; the percentage in that category had been increasing steadily in the South, from 36 percent in 1880, to 47 percent in 1900, and reaching the 50 percent mark by 1910.

Farm tenancy and a related share-cropping system was devised in the immediate post-Civil War years when the plantation system could not be revived, and farm land values in the absence of an assured labor supply plunged in price. Credit to producers for seed, fertilizers and groceries from one crop to the next could be obtained only by committing to lenders a cash crop, such as cotton, which could not be consumed by the grower and which always would be accepted in world markets. Within two decades the major segment of regional agriculture was enmeshed in an essentially pernicious system.

Although the socioeconomic effects of tenancy and share cropping were detrimental to the region's long term best interests, individual farmers could utilize the system with maximum effectiveness for the welfare of land owner and land user alike. Elizabeth Allston Pringle illustrates the application of successful business practices in the ownership and management of a small rice plantation in post-bellum South Carolina. Mrs. Pringle, a widow, purchased an approximately 200 acre farm in 1880, for $10,000, half cash and half on mortgage, and spent about $5,000 on mules, equipment and supplies. Lacking any working
capital, Mrs. Pringle decided to plant 50 acres on wages and 150 acres on shares, giving to croppers only seed and asking for 10 bushels of rice to the acre, with all above that level going to the croppers. With the aid of a foreman, she supervised production during the first planting season, encouraging both wage workers and croppers. The system worked extremely well and for the next four decades, as her diary reveals, she planted annually from 20 to 30 acres on wages and rented the remainder. In the early years Mrs. Pringle relied primarily upon the experience of her father, a successful rice grower, and upon the practices and family legends of a great aunt, a spinster whose success in managing rice acreage had become a community legend. Over the years, in attaining consistently higher yields and better financial returns than her neighbors, Mrs. Pringle's greatest asset most likely lay in her effective application of productivity incentives and share cropping practices which benefited mutually both parties to the arrangement.

While rice and cotton relied heavily on crop sharing, tobacco, the region's third major cash crop, was cultivated more commonly by land owners. As a labor intensive crop, tobacco could be grown readily in conjunction with a variety of other farm commodities. The shift in tobacco production from the upper south to Kentucky, Tennessee and North Carolina encouraged a trend toward diversification in those states. By 1890, Kentucky produced more tobacco than Virginia and Maryland combined. That state held premier rank until 1927 when first place was yielded to North Carolina. The Tarheel State's dominant position was attributable to the expanding demand for cigarettes and the consequent shift to the production of bright leaf, flue-cured tobacco which thrives on her soil. It is not surprising that the tobacco producing states, characterized by small scale farming, also led the region in agricultural diversification.
Other major factors which loosened the grip of monoculture within the region included the introduction of the refrigerator car and the devastating effect of the boll weevil. In 1872 the first refrigerator car load of strawberries from the lower Mississippi Valley reached Chicago and generated expanding interest in fruit growing and truck farming in various parts of the region. Shipments of pecans, fresh citrus fruit from Florida and peaches from Georgia and South Carolina opened new opportunities for agribusiness in the region. By 1900 Georgia was growing more than 21 million watermelons annually, primarily for consumption in large northeastern cities. About that time, the boll weevil, which in 1892 had crossed the Mexican border into Texas to begin its inexorable march eastward, surmounted the Mississippi River barrier and began to ravage regional cotton crops. In time the tiny snout beetle was to topple from their regional perches both King Cotton and the interior furnishing merchant who emerged as the most feasible mechanism to finance cotton cultivation and distribution.

In the post-bellum era, the penetration of the railroad network into the interior, along with the telegraph, led to a concentration of the purchase of regional cash crops in the interior. Virtually every stop on trunk line regional railroads emerged as a distinct market where the grower could dispose of his crop. The result was a flowering of interior towns and villages where furnishing merchants supplied credit and merchandise to planters and share croppers within the surrounding countryside and where each autumn cash crops were purchased and shipped in order to redeem year long debts. A major ramification of this development was the decline of the seaport oriented cotton factorage system in which the up-country pre-Civil War general store served as an adjunct.
After 1865, with the failure of the shortlived experiment with plantation wage labor, the larger land owners, with access to northern dry goods and food wholesalers and fertilizer dealers, gradually evolved into furnishing merchants for tenants and croppers on their land. Some continued dual planter-merchant practices; others gradually permitted the mercantile side of the business to predominate. The reverse process also took place in which aggressive operators of up-country general stores severed their dependent relationship with seaboard factors and greatly broadened the scope of their mercantile operations. Some acquired land and began to cultivate cotton through contracts with share croppers or with rent paying tenants. The more dynamic of the group rose above the small businessman status and introduced new business methods, such as farm commodity shipments on through bills of lading and speculation in the futures market.

Much has been written of the exploitive tactics of furnishing merchants of the 1865 to 1920 era. They did, indubitably, charge higher prices on store goods sold on credit and did charge high interest on farm credit balances. Nonetheless, in the absence of an adequate farm credit system, they did perform a vital function in making available necessary credit. Furthermore, their acceptance of lien notes in early spring upon crops yet to be planted involved considerable uncertainty, including the hazards of a fickle regional rainfall pattern and the vagaries of oftentimes insufficiently motivated croppers. Not to mention the steady decline of commodity farm prices during the last third of the 19th century. Prices improved after the turn of the century, but by then the boll weevil introduced a new and more terrifying element of risk. In fact, the impact of the general store and its credit granting proprietor peaked just prior to World War I. The weevil was only the last of several adverse elements which were to seal the fate of this significant segment of the regional business community.
During the final decades of the 19th century, as farm proprietors struggled to remain solvent and small town merchants served those working the land under varied legal arrangements, the region's manufacturing sector began to surge. The accelerated industrial growth was spearheaded by native entrepreneurs, usually with limited financial resources. The initial emphasis was placed upon the processing of locally abundant raw materials, for a regional and eventually a national and world market. An additional attraction to nascent manufacturers was the availability of low cost labor, although most were farm reared workers unfamiliar with factory discipline. Initial financial requirements were met, in notable instances, through the cooperation of northern machinery makers and commission merchants, anxious to sell equipment and gain distribution rights of regionally produced output.

Cotton textile manufacturing was the industry that sparked the regional take-off to economic growth. Cotton production had established strong ante-bellum roots in a number of locations, but the entire South in 1860 operated fewer than 7 percent of the nation's spindles. Furthermore, few regional mills survived destruction of the Civil War.

A number of entrepreneurs who launched enterprises during the "cotton mill crusade" of the 1880 to 1900 era were established members of the middle class. Robert I. McCaughrin, foremost promoter of Newberry Mills in South Carolina, was proprietor of the town's leading dry goods store and head of the local bank. H. M. Comer, a successful Savannah-based cotton factor, was one of three stockholders in Bibb Manufacturing Company, of Macon, Georgia. Many of the pioneer regional millmen were young men reared in the countryside with a strong background in sales. Fuller E. Callaway as a boy of eight began peddling spools of thread to farmers' wives living on the outskirts of his home town, LaGrange, Georgia. Bobo Simpson Tanner as a young man clerked in several stores and then
for a dozen years was a drummer on the road for the Elias and Cohen jobbing house. In this capacity he learned the kinds of cloth designs his future customers preferred and the prices they were willing to pay. James B. Cannon, born in a farmhouse near Sugar Creek Church in Mecklenburg County, North Carolina, at age 14 began clerking and running errands in a Charlotte grocery store, and later acquired an interest in a general store in Concord which was co-partnered by his brother. Not until he was 35, in 1887, did Cannon make the decision to begin textile manufacturing. His 4,000 spindle mill was completed the following year; Cannon was general manager and sole salesman for its output.

Neither visionary nor idealistic, the pioneer promoters of the region's post-bellum cotton mills were venturesome small businessmen. Excelling in the low cost production of coarse cloth, they spearheaded the region's leadership in electrifying plants, adopted modern equipment more quickly than their New England counterparts and expressed an early interest in developing the export market.

The region dominated the developing southern textile industry. Within the region cotton production was heavily concentrated within four states: the Carolinas, Georgia and Alabama. In 1880 these states contained 119 of the 164 mills operating throughout the South, and 422,000 of its 561,000 spindles. Georgia, in 1880, was the region's foremost state in numbers of spindles, although North Carolina held premier rank in the number of mills. By 1910 these four states had strengthened their relative position in the industry. They now contained 637 of the South's 731 mills and operated more than 10 million of the South's 11.2 million spindles. North Carolina in 1910 had more mills than its two closest competitors combined; South Carolina had moved into first place in terms of spindles in place. By 1910 the industry had become
heavily concentrated in the piedmont portions of the leading states, where access to water power and an abundant labor supply were important locational advantages. The industry remained locally owned and managed. A 1922 study disclosed that 84 percent of southern cotton mill spindlage was owned or controlled by southern capital.

Measured in terms of value added by manufacturing, the region's most important industries at the turn of the century, in addition to textiles, were lumber processing, food manufacturing, primary metal fabrication, especially in Alabama and Tennessee, furniture making, especially in North Carolina, stone, clay and glass making, and tobacco processing. Printing and publishing was important although the region's kraft paper industry was yet to develop. The apparel industry was growing, although still relatively small.

The essential characteristics of the region's leading manufacturing industries stamped them as ideal small business ventures. Most of them had no limits upon entry and had modest capital requirements. They involved the processing of readily available raw materials or locally produced agricultural commodities. Optimal efficiency could be attained at relatively low levels of production. For most industries labor costs constituted an important component of total costs, but employee requirements could be met primarily with low skilled male manual workers and semi-skilled females. Measured in terms of industry concentration, most regional industries were highly competitive. A notable exception was tobacco processing, which under the dynamic leadership of James B. Duke of North Carolina was being converted into one of the nation's oligopolies, dominated by Duke's American Tobacco Company.

The resource-intensive character of regional industry was not to be reversed until the post-World War II period. Harriet Herring in her carefully researched *Southern Industry and Regional Development*, published in 1940,
concluded that virtually all the South's leading industries were "based directly or indirectly on some crop or natural resource either peculiar to the Southeast or found more plentifully in that region than in other parts of the country."

Herring's study disclosed that on the eve of World War II only a limited number of regional manufacturing industries in terms of employment were producing for a national market. These included: cigarettes, cotton yarn and woven goods, rayon and allied products, fertilizers, cast iron pipe, lumber and timber products, hosiery, men's trousers and work clothing, knitted underwear, cordage and twine, distilled liquors, nonalcoholic beverages, cooperage, paper bags, and office and household furniture. The structure of a number of the more capital intensive industries--cigarettes, rayon, cast iron pipe, paper products--had become dominated by a few large firms. Many industries, however, remained characterized by a large number of small scale enterprises. Small business dominance also was the hallmark of many of the manufacturing industries which, in terms of employment, served the regional market primarily. These included confectionary products, men's shirts, caskets and coffins, book and job printing, drugs and medicines, and the making of brooms, mattresses and bedsprings.

The accelerated growth of regional industry in the years after 1880 was spearheaded primarily by native-born businessmen. Although proponents of the New South urged that intensified efforts be directed to encouraging immigrants to the region, their efforts were successful only to a small degree. In 1899, only 51 persons of the millions landing at Ellis Island listed North Carolina as their destination. Within the region, Florida, still in a pioneer stage, had the greatest appeal to newcomers; 2,690 listed that state as their destination.

Despite their small numbers, first generation Americans made a proportionately large impact upon the economic development of the region, and especially upon the growth of small business. The limited number of immigrants who made a
voluntary decision to locate in the region did so often with the purpose in mind of engaging in business activity. They regarded the region as an area of the nation in which competition was less intense, capital requirements were low and where assimilation and upward mobility could be attained within one generation. In considerable numbers of cases they were correct in this assessment.

A study by Robert Higgs dealing with the "Participation of Blacks and Immigrants in the American Merchant Class, 1890-1910," published in Explorations in Economic History in 1976, disclosed that in every state in the region, in every time period, the number of male retail merchants per 1000 gainfully occupied males was significantly higher for foreign born white males than for either native born whites or for black males. The relative importance of foreign born merchants to total male employment was greatest in Mississippi, South Carolina and Georgia. It was least significant in Florida, Tennessee and Kentucky, although even in those states the contrast with native white merchants and black merchants was great. A comparison of merchants in major cities revealed a similar large differential. For Atlanta in 1910 the numbers of merchants per 1000 employed males were 229 foreign born white, 64 native born white and 15 black. For Louisville, the numbers were 134, 51 and 12 respectively; for Memphis the numbers were 193, 69, and 13 respectively; for Nashville, they were 247, 71, and 17 respectively. A major finding of Higgs was that for immigrants the rate was "substantially higher in the Southern than in the Northern cities."

The number of black retail merchants in relation to total male employment, as disclosed in Higgs' study, was far smaller than that for either foreign born whites or native born white merchants. Higgs concludes that business opportunities for blacks "played a relatively trivial role" in that group's effort
to enter the mainstream of nation's economy. Nonetheless, especially in view of the obstacles faced by blacks in agribusiness and urban business pursuits, the magnitude of their effort is impressive.

Despite the disappointment of rural blacks who had hoped to obtain land and working stock from the government along with their freedom, some were successful in securing title to land. A 1876 Department of Agriculture survey disclosed that black farmers had acquired approximately 4 percent of all land held in Alabama and Tennessee, 4 to 5 percent in North Carolina and Georgia, 5 percent in South Carolina, 5 to 6 percent in Mississippi and 8 percent in Florida. A case study of a single Georgia county disclosed that black-owned acreage doubled between 1874 and 1894 and continued to grow until World War I. Another study revealed that in 35 cotton belt Georgia counties black-owned acreage doubled between 1899 and 1919, before declining after the boll weevil struck. Black farmers in South Carolina also increased their land ownership and improved their farm practices through the first two decades of the century, benefiting from the work of the state agricultural colleges and from the efforts of country agents under the Smith-Lever Act of 1914. In 1920, black farmers in South Carolina owned 1.1 million acres, an average of 63 acres per farm. After 1920 a combination of factors led to a decline in black farm ownership.

Black entrepreneurship in the non-agricultural sector was also more effective outside the larger cities. Booker T. Washington, making an extensive survey of The Negro in Business, published in 1907, found that he was "constantly surprised to note the number of colored men and women, often in small towns and remote districts, who are engaged in various lines of business."

The first authoritative study of black business was conducted by W.E.B. Dubois in conjunction with a conference on black problems held at Atlanta University in 1899. Using the 1890 census, Dubois estimated approximately
5,000 black businesses in the nation. For the 8-state SBA region #4 DuBois recorded 1,040 black business enterprises. Georgia had the largest number, 324; the states with the smallest numbers were Kentucky, Mississippi, and Florida, with 72, 78 and 78 firms respectively. DuBois, conceding that many smaller towns and country stores were omitted in his survey, found that the most successful ventures were in personal services: barbers, restaurant owners, caterers, expressmen. He concluded that the main variables in determining the number of black businesses were the density of black population and black experiences with business under slavery. Not surprisingly, the DuBois study disclosed that the fewest number of black businesses were in the "capitalist" class: bankers, real estate dealers, building and loan associations, and manufacturers, although he did locate a few black firms making shirts, brooms, fans and carpets.

On the case study level, numerous studies of black business have depicted individual success stories, including a small number of firms which succeeded in developing a bi-racial clientele. And there were even some rare cases of white business promoters soliciting the aid of blacks with special skills, such as young George Washington Carver at Tuskegee Institute assisting a group of white Alabama promoters establish a paint factory using local mineral deposits. But these instances were exceptions to a general pattern in which increasingly after the turn of the century, with a more rigidly segregated, regional society, black businessmen were deprived of the white market and were increasingly forced to rely on "racial pride" to retain their black customers.

As Harry Golden later reminded listeners, a ghetto can serve as a fortress as well as a prison. Some black businessmen did benefit from the fortress mentally, obtaining the trade of black customers unwilling to endure the degree of humiliation sometimes associated with shopping at white owned
establishments. As the limited receipts of most black businesses demonstrated, most members of the black middle class preferred to patronize the typically larger, better organized and sometimes more sanitary white owned establishments. A National Negro Business League Study in 1928 of 1,500 black retail stores throughout the nation disclosed that 63 percent had annual gross receipts of less than $10,000; on the average, they employed fewer than 4 persons. Within the region, the average black establishment had smaller receipts and fewer employees.

In his perceptive assessment of the barriers to black business success, V.V. Oak, in *The Negro's Adventure in General Business*, published in 1949, placed some weight on the difficulty of black businessmen in obtaining adequate capital and credit for expansion. But he placed greater emphasis upon their difficulty in obtaining trained and honest management, capable of understanding the operation of the business as well as consumer psychology and willing to perform hard work for long hours.

The capital needs of black businesses were met in part by the establishment of numerous black owned banking institutions. The first to be organized in the region was the Mutual Bank & Trust Company established in Chattanooga, in 1889. The following year the Alabama Penny Savings & Loan Company was started in Birmingham. The Mutual was unable to survive the panic of 1893, but the Birmingham bank lasted until 1915. Between 1899 and 1905 at least 28 black owned banks were opened in various southern cities primarily to serve as depositories for fraternal orders. By the end of 1905, only 7 had survived.

Although many of the pioneer black banks were launched in order to supply struggling black businesses with credit, the vast majority of small, family owned enterprises, in the leisure time, amusement and personal service fields, did not seek capital for improvement or expansion. As a result, many of the
black banks which failed possessed frozen and depreciated real estate holdings among its most important assets. E. F. Frazier, in Black Bourgeoisie, attributes the "unproductive use of credit" as being the major factor in the high failure of black owned banks. The study of black banking by Abram Harris, The Negro as Capitalist, published in the mid-1930's, disclosed that between 1889 and 1934, 64 black owned banks were organized within the region. The largest number were started in Georgia, 14; Mississippi had 12 and North Carolina, 11. In 1928, on the eve of the Great Depression, the total resources and liabilities of black banks in the region ranged from $98,500 in Alabama to $1,221,000 in North Carolina. In 1934, 23 black banks were functioning within the region. Harris' analysis of the large number of bank failures concluded that the banks tended to have too large a capital structure for the amount of business conducted and that the security behind the loans and discounts was too often either real estate or chattel property.

Perhaps the most successful sector of black business in the region revolved around the sale and servicing of low premium, limited protection life insurance to a black population deeply committed to being assured a decent Christian burial. Industrial life insurance had been introduced into the United States in 1875 by the Prudential Insurance Company and within a decade southern based white-owned enterprises were established to market burial policies to white and black customers. In 1891, two rural bred north Georgia entrepreneurs, J. N. McEachern and I. M. Sheffield, organized under Alabama insurance codes an enterprise that was to become one of the region's largest, Life Insurance Company of Georgia. From the beginning it sold contracts exclusively to a black clientele. Soon thereafter, black insurers, linking the financial motive with an uplift goal, evolved out of numerous church related and fraternal organizations which provided life and health insurance protection to their members.
The two most important regional black owned commercial insurance companies were both organized principally through the efforts of successful black small businessmen and received early encouragement by white capitalists. North Carolina Mutual Life Insurance Company was started in Durham, in 1898, by John Merrick, a bricklayer and barber with a wealthy white clientele, who became aware of the insurance needs of improvident blacks. Assisted by a local black physician and aided by a number of wealthy whites, including James B. Duke, North Carolina Mutual was launched successfully and grew steadily through the efforts of a number of competent black businessmen, including C. C. Spaulding. Atlanta Life Insurance Company was organized in 1905 by Alonzo Herndon, a former slave who operated an elite barber shop for a white clientele. Approached by a group of black ministers who urged him to take over and conduct on a commercial basis the operation of a benevolent society they had begun, Herndon agreed and commenced by selling weekly premium policies exclusively. In 1927, the Atlanta Life moved into the higher income market by selling ordinary life insurance.

A 1929 survey of "Insurance Business Among Negroes," by C. G. Woodson, disclosed 11 black owned legally organized life insurance companies headquartered in the region. They marketed their contracts exclusively among the black population and vied with a number of northern-based insurers as well as several score small white owned regionally based companies which were selling and servicing life and health insurance on the Home Service weekly premium plan either to an exclusively black clientele (as with Life of Georgia) or to the region's total bi-racial market.

4. SMALL BUSINESS IN AN ERA OF ACCELERATED GROWTH, 1940-Present

World War II served as a watershed for the region, moving it much closer to the mainstream of national social and economic life. The acquisition
of industrial knowledge on the part of management and labor, the rise in per capita income and purchasing power, the increase in the level of savings and the accumulation of capital all interacted to create a highly favorable environment for further post-war advances. The region's predominately rural residence pattern was also altered as the war gave a great impetus to urban growth, with port cities registering especially high gains. Mobile's population increased 68 percent and Charleston's 57 percent during the war years.

Expanding per capita incomes led to a sharp growth in purchasing power and, once the war ended, resulted in a surge in retail sales. Between 1939 and 1947, the Atlanta district of the Federal Reserve Bank increased retail sales by 232 percent compared to a national average increase of 158 percent.

Higher incomes of regional farmers and workers led to a significant growth in the level of savings. Assets of southern commercial banks grew by more than 200 percent from 1939 to 1947, compared to an increase of 131 percent in the non-South. Southern based life insurance companies increased their premium income, assets and life insurance in force markedly during and immediately following the war years, thus mobilizing resources that were to assist in financing a surge in regional urban real estate construction in the post-war period. War Production Board chairman Donald M. Nelson had these favorable trends in mind when he informed an Atlanta audience in Spring, 1944: "The South is no longer America's economic problem number one, but America's economic opportunity number one."

The expanding opportunities afforded regional businessmen were made possible by sharp increases in per capita income, rather than any significant growth in total population. Indeed, during the post-war decade with the most rapid population growth rate, 1950-1960, only Florida outpaced the nation. During the 1950's and 1960's the region continued to export lower income persons...
while attracting a smaller number of higher skilled, higher income individuals. Per capita income in the region which stood at about one-half the national average in 1900 and about three-fifths the national average in 1940, climbed to three-fourths national average by 1960. The regional income gap continued to close and by the mid-1970's studies of per capita disposable income adjusted for differences in the cost of living across various states indicated that one state (Florida) exceeded the national average, that the state with the lowest adjusted per capita income (Mississippi) was 79.2 percent of the national average and that most states in the region ranged between 88 percent and 95 percent of the national income.

The significant upswing in regional per capita income was accompanied and was greatly facilitated by a sharp decline in regional farm employment and a significant improvement in productivity and income for those remaining on the land. John Gunther, in his perceptive survey of the nation, Inside U.S.A., written immediately following the war, made the flat statement: "Overwhelmingly the South is rural." The great exodus from the region's countryside, however, had already begun. Between 1940 and 1950 Alabama's black population dropped from 48.6 percent rural to 32.5 percent rural, Mississippi's from 72 percent to 60.1 percent, South Carolina's from 60.3 percent to 45 percent. With the mechanization of cotton production and the trend toward more capital intensive and diversified agriculture, the exodus accelerated. In 1977, farm employment in Alabama was 86,000 compared to 277,000 in 1950; in Mississippi it was 88,000 compared to 459,000; in Tennessee it was 131,000 compared to 363,000. Many of those who retained rural residences remained farmers only nominally as they became employed in non-agricultural occupations. Those who remained in regional agricultural were able, on the average, to increase their incomes considerably. Between 1950 and 1977 total cash farm income from marketing and government
payments rose in the region more than threefold. In Alabama the increase was from $368 million to $1.6 billion; in Florida, from $569 million to $2.5 billion; in Georgia, from $458 million to $2.2 billion; in Tennessee, from $438 million to $1.4 billion.

In some instances the increase in income was accompanied by a growth in the scale of farm operations which brought the enterprise into the medium or large-size category. But such instances were atypical. The diversified character of farm operations, the labor requirements, assets and income received, placed the great majority of regional farm units firmly within the small agribusiness category.

Pacing the diversification of regional agribusiness since the close of World War II has been the great surge in soybean production, a shift in land use toward livestock raising and poultry and egg production, and a sustained expansion of peanut and citrus fruit production. Soybean production in the Southeast has grown from 38.4 million bushels in 1950 to 456 million bushels in 1977; the growth rate has been especially high in Mississippi, Tennessee and Alabama, where the construction of large export elevator facilities at Mobile has stimulated production in the south central part of the state. Advocates of agricultural diversification have long preached the climatic and physiographic advantages of the region to the livestock industry. A modest movement toward the region accelerated in the 1950's, particularly in Tennessee and Florida. The growth of regional farm receipts from livestock has been especially great in the 1970's, attaining a level of $8.6 billion in the Southeast in 1977, or 18 percent of the national average. (This compared with 11 percent of the national average in 1950.) Broiler production in the Southeast has increased from 37 percent of national output in 1950 to 68 percent in 1977. In that year, Georgia and
Alabama together produced more than one-fourth of the nation's 3.4 billion broiler chicks, with most small regional producers operating on a commission basis for large national processors and distributors of the final food product.

A significant 1976 study of white and black small farmers in the 13-state South, conducted by James Lewis for the Department of Agriculture, illuminates recent regional trends. Classifying small farmers as those with less than $2,500 worth of agricultural products sold, Lewis found that in 1969 this group consisted of 49 percent of all southern farm operators. They owned about 20 percent of the land owned by southern farm operators and held about 19 percent of all southern farm machinery and equipment. Minority members of this group, primarily black, represented 7.9 percent of all farm operators and controlled 2.4 percent of all land in farms. The Lewis study disclosed that while white small farm operators in large numbers have shifted their operations to livestock, poultry and dairy production, minority farm operators have been slower to change. Lewis suggests that the slower response of minority farmers to market signals could be caused by smaller scale operations, lack of adequate information, more difficult access to capital or reluctance to break away from traditional production processes. Lewis also cites a 1974 Census report on farm population which discloses a significant trend toward multiple job holdings among low income regional farm residents. In 1973, 53 percent of southern farm resident members of the labor force were engaged in non-agricultural industries; this compared with 45 percent among farm residents outside the South.

Rural and small town industrialization in the region has been gaining momentum since the 1920's. President Hoover's Committee on Recent Economic Changes, in calling attention to the "rapid industrial growth of the South," focused on "the shift from city to country." The records indicate, the Committee reported, "an actual gain in the rural areas," particularly in the
East North Central and the South Atlantic divisions. The depression decade of the 1930's accelerated this movement, especially in labor intensive industries such as textiles and apparel, seeking lower labor costs. The war years reversed the trend with the concentration of government contract work in the port cities and larger urban centers. But in 1947, John Gunther, in noting that "The South has considerably more industry than most people give it credit for having," also perceived the potential of travel and tourism in attractive parts of the region other than south Florida and the Gulf Coast resort communities.

A major force propelling regional economic growth after World War II was the expanding southern market. The National Planning Association's 1949 study, Why Industry Moves South, concluded that favorable market opportunities was the major motivation for businesses moving to the South in 45 percent of the cases. Thirty percent of the relocations were due to raw materials and energy considerations; 25 percent were attracted principally by labor availability and cost. Industrial market oriented plants included paint and lacquer, synthetic fibers, treated lumber, cans and bottle caps, sole cutting for leather goods, commercial envelopes and paper boxes, and textile and open mesh bags. Consumer market oriented plants moving into the region included auto assembly plants, batteries and lamps, candy, dog food, farm equipment machinery, tires and tubes, and asphalt tile for building materials. Whether directed toward the industrial or consumer market, firms which migrated to the region anticipated obtaining economic benefits by minimizing transport costs, offering better service and customer convenience, and gaining the loyalty of the local community. Although the study purposely omitted a large group of small market oriented plants supplying a range of perishable and other goods to the region, the medium and large sized national firms whose moves were studied soon generated a multiplier impact by subcontracting with local firms and, through enlarged
payrolls, significantly enhanced the purchasing power of the surrounding area.

With the influx of higher wage market and raw material oriented industries, the structure of the region's manufacturing sector began to shift. The traditional, primarily lower wage industries continued to grow but at a slower pace. Textile employment in the four dominant states of the region (the Carolinas, Georgia and Alabama) increased from 525,000 in 1950 to 590,000 in 1970. As northern mills closed down or moved their operations to the South, these four states increased their share of national textile employment from 41.9 percent to 60.6 percent. By the early 1970's, the nonmetropolitan concentration of textile employment ranged from 70 percent in Georgia to 86 percent in North Carolina, the nation's leading textile state, with 28.8 percent of total industry employment in 1970. The industry also trended in the direction of larger scale production, dominated by a limited number of medium size firms able to engage in research and promotional activities. A 1967 study disclosed that 6 percent of the region's textile establishments with 500 or more workers employed 45 percent of the industry total. A large number of small firms, however, remained in the region. In 1967, one of every three mills employed fewer than 20 workers and 60 percent of all mills employed fewer than 50 workers.

Among labor intensive industries, the region also increased its relative share of apparel employment. In 1950, the five leading states in regional apparel production (Carolinas, Georgia, Tennessee and Alabama) employed 7.4 percent of the nation's clothing workers; by 1970, they held 22 percent of the nation's apparel employment. Even more so than textiles, the apparel industry was characterized by small scale operations and employed large numbers of female workers. Both industries significantly relied upon black workers in the period since the 1954 Supreme Court desegregation decision.
More significantly, the region increased its relative share of the nation's employment in a wide range of capital intensive, higher wage paying industries. Included in this category were the man-made fiber industry, transportation equipment, food products, leather goods, paper and allied products, and the furniture industry. The last named industry made such heavy gains in employment within the region that the United Furniture Workers of America, an AFL-CIO affiliated national union, made the decision in August, 1979 to transfer its headquarters from New York City, where the union was based for 45 years, to Nashville.

During the two decade era of most rapid growth, from 1953 to 1972, manufacturing employment in the 8-state region increased from 1,895,800 to 3,185,000. In terms of total non-agricultural employment in the region, however, the share maintained by manufacturing declined from 33 percent to 29 percent. Although it is not possible to quantify with precision the degree of difference, it appears certain that the relative share of manufacturing employment in the region held by medium- and large-size enterprises increased during the twenty year period.

Government employment, particularly local and state employment, also grew rapidly in the region from 1953 to 1972, from 886,300 in 1953 to 1,985,000 in 1972. Government employment as a percentage of total regional non-agricultural employment grew from 15.4 percent in 1953 to 18.1 percent in 1972.

A closer scrutiny of the changing composition of the regional economy during the 1950's and 1960's discloses that the great growth in non-farm employment, from 5,750,700 in 1953 to 10,980,000 in 1972, was concentrated neither in manufacturing nor in government employment. The two combined decreased their share of total non-farm employment from 48.4 percent in 1953 to 47.1 percent in 1972. The great increases in employment took place in the trade, services,
financial and construction segments of the regional economy. These were industries in which, quite different from manufacturing, average firm size remained small.

An assessment of all establishments in the state of Tennessee, by industry and employment size, for 1976, typifies the regional structure of employment. Of 5,528 establishments in manufacturing in Tennessee, 187 had 500 or more employees. The number of establishments in other Tennessee industries, followed by the number with 500 or more employees were: wholesale trade, 6,992 and 3; retail trade, 24,204 and 11; finance, 6,788 and 10; services, 20,753 and 39; construction, 7,604 and 2. It is clear from this breakdown of the number of establishments in each industry and those with more than 500 employees that the vast majority of workers in a wide range of non-agricultural industries were employed by small rather than medium or large businesses. A similar small business dominance can be documented in mining and in transportation, but these industries were omitted from analysis because of the smaller numbers of employees involved.

With the point established that non-manufacturing employment in the region is very largely concentrated in small firms, a comparison of employment in trade, services, finance and construction between 1953 and 1972 can shed some light on the trends affecting small business in the region during this significant twenty year period.

Personal employment in retail and wholesale trade increased from 1,295,300 in 1953 to 2,315,000 in 1972, or from 22.5 percent to 21.1 percent of non-farm employment. The most significant development in this sector during the 1950's and 1960's was the great growth in franchised enterprises, especially convenience stores and fast food outlets, offering opportunities for individual owners to minimize risk through an association with a large national firm. A number of
franchises were initiated by entrepreneurs within the region and a preponderant number of outlets has been located in the sunbelt. Munford, Inc., based in Atlanta, had by 1979 1,300 outlets in a 15 state area. The 7-Eleven chain, owned by Southland Corporation in Dallas, was started in 1927, but only in the 1950's began rapid expansion, primarily at first in Texas and Florida. By 1979, it operated more than 7,600 stores, one-third of them franchised. In 1951, Col. Harland Sanders founded his Kentucky Fried Chicken chain in Corbin, Kentucky, and began to franchise outlets primarily in the southeast. By 1960 Sanders had 200 outlets. The chain was sold in 1963 to a group formed by Kentucky entrepreneur John Y. Brown who resold it eight years later to Heublein, Inc. By 1979, there were 5,138 KFC outlets around the world, about 4,000 of them owned by franchisees. The corporation has established a school in Louisville to provide refresher courses for store managers and franchisees. The growth of franchising in Georgia is illustrative of developments throughout the region. In the mid-1970's there were 1,207 fast food restaurants, only 150 fewer than in New York State, with four times Georgia's population. There were also company or franchisee operated 49 printing and copying shops, 1,664 convenience stores, 227 motels and hotels, 27 campgrounds, 136 dry cleaners and laundries, and 93 car and truck leasing firms.

With the steady erosion of family owned groceries and the difficulties encountered by small dry goods stores and specialty shops in competing with the surge of self-service discount department stores the rapid expansion of the franchise concept has enabled the retail trade sector to maintain its relative position as the region's second most important employer. Notable also is the fact that franchising has made a more extensive contribution to black capitalism in the region than any other single factor.
The sectors of the regional economy which experienced the greatest
growth rates in employment between 1953 and 1972 were in services and in the
finance-insurance-real estate sector. Both categories are heavily weighted
toward small scale enterprises. During the two decades regional service
employment increased from 572,000 to 1,579,000, or from 10 percent to 14.4
percent of total employment. During this period employment in the regional
financial-insurance-real estate sector grew from 185,000 to 519,000 or from
3.2 percent to 4.7 percent of total employment.

Travel and tourism in the sunbelt states provided a strong impetus for
regional growth in the service sector. Acquiring franchises to operate motels
and adjacent restaurants and service stations constituted an important area
of opportunity for small business enterprise during the quarter century from
1950 to the mid-1970's. One of the motel chains in the region to grow most
rapidly was started by Cecil Day of Atlanta. Days Inn, a no-frill, low priced
motel concept, caught the fancy of a cost conscious public. By summer, 1978
there were 100 Days Inn locations, primarily throughout the region, 98 of
them franchise owned.

The growth of the financial sector in the region was highlighted by the
expansion of regional banks and insurance companies, many launched much earlier
but relatively stagnant until the surge of regional business activity and the
improvement in per capita income in the period after 1950. The growth of
smaller regional banks included black owned commercial institutions. In 1945
there were approximately two dozen black owned Savings and Loan Associations in
the South with combined assets of about $10 million; by the early 1960's,
the number had grown to 45, with assets totaling about $300 million. Among
the region's approximately half dozen black commercial banks, Citizens Trust
Bank of Atlanta by the early 1960's had more assets than all black banks
combined had in the first year of Franklin Roosevelt's administration.
One of the most significant developments in the realm of small business since the end of the World War II has been the increasing participation of women and minority groups in regional business. In 1976, a pioneer statistic compilation entitled, Women-Owned Businesses, 1972, disclosed that there were in that year 63,150 firms owned by women in the region. They employed just under 40,000 workers and had gross receipts of $1,358,397,000 or an average of $21,510 per firm. The state with the largest number of firms owned by women was Florida, with 18,542 firms and $371,000,000 gross receipts in 1972. A breakdown of minority women owned enterprises revealed that in 1972 there were 6,435 such firms with total employment of approximately 5,000 and with gross annual receipts totaling $166,404,000, or approximately $25,860 per firm.

A more comprehensive count of minority owned businesses, conducted by the Census Bureau in 1971 disclosed that in 1969 there were 46,882 minority owned firms in the region with gross receipts of $1,332,900,000 or $28,430 per firm. The state with the largest number of minority firms was Florida with 12,557, followed by North Carolina, 8,017 firms and Georgia, 7,086 firms. The average number of employees per firm was small, ranging from 3 employees in Mississippi and South Carolina to 5 employees in Alabama and Tennessee.

The impact upon the region of the Hispanic group is revealed in a special Census Bureau report on Minority-Owned Businesses, Spanish Origin, published in 1975. The impact was greatest, of course, in Florida, where in 1972 Hispanic owned firms (primarily Cuban) totaled 6,726 in number. The firms employed 12,306 persons and had gross receipts of $447,896,000. As the Cuban immigrants began to spread to other states, by 1972 there were more than 1,000 Hispanic owned firms outside of Florida, throughout the region.

In more recent years, numbers of Vietnamese and Russian Jews have settled in various communities throughout the region and have begun in
considerable numbers to establish small business enterprises. Indicative of this trend are two restaurants in downtown Atlanta, with a small grocery store separating them; they are a "Cozy Diner" run by a middle-aged husband and wife, Russian refugees and a small restaurant featuring Vietnamese food, run by a young, recently arrived couple. Future statistical tabulations will document their contribution to the continued growth of small business in the region. Their presence vividly illustrates the sustained viability of small business in the region as a vehicle for sturdy self-support while performing a welcomed service to their clientele and to their community.
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1. INTRODUCTION

Without any data, the safest guess one could probably make about small business in Region IV is that profits are below average. Such a guess would, of course, be based on the region's well-known below-average per capita income. What data is available confirms this guess. Those not familiar with the South's recent past might also guess that the region's small businesses are growing relatively slowly and are much more likely than elsewhere to be engaged in agricultural pursuits. This is hardly the case.

Interstate structural differences between Region IV's small businesses exceed those between the region as a whole and the nation. (Structure refers to the relative importance of the various industries.) Interstate differences are largely based on such geographic factors as location and natural resources. Structural differences between the region and the nation are largely due to comparative advantages which are related both to geographic and other factors. For example, a milder climate and lower wages have attracted industries to the region, but all industries have not been equally attracted because of their varying needs. Southern entrepreneurs are, due to the relatively less developed nature of the region, the "new boys (and girls) on the block;" thus, they gravitate to fields where new firms have the best chance of success.
Structural differences and the age of the average firm will affect the size of the average firm's sales, profits, payroll, and employment. Market size, too, will have an effect. The firm which serves more than the local market will normally have greater sales than one in the same industry which only sells locally. The size of local markets, of course, varies enormously. Often the local market isn't large enough to absorb the output of the smallest manufacturing plant large enough to obtain the economies of scale necessary to compete with outside competition. The smallest viable manufacturing operation is larger than in other industries due to the greater possible economies of scale. In contrast, a provider of services, who often must be physically close to his customers, can be quite small and still be competitive. Expansion of a service firm is more likely to mean setting up a new establishment instead of enlarging an existing establishment. New firms in any industry will usually have fewer employees than an older firm. Returns to owners and employees differ between industries. Wages are highest in mining and lowest in services. All of these differences, and more, play a role in explaining differences between regional and national averages for all establishments.

2. PROFILE OF SMALL BUSINESS IN REGION IV

As employers, small businesses (establishments of up to 500 employees) are more important in Region IV than they are in the nation as a whole. As is the case for the nation as a whole, small establishments have in recent years become more, rather than less, important as employers. See Table 1. The rising share of total employment accounted for throughout the nation by white collar occupations and the falling share accounted for by blue collar manufacturing jobs, plays a role in this change. Note, however, that in some
Table 1

PERCENT OF LABOR FORCE EMPLOYED IN FIRMS EMPLOYING
500 OR FEWER WORKERS*
UNITED STATES AND REGION IV STATES
1970 AND 1976

<table>
<thead>
<tr>
<th></th>
<th>1970</th>
<th>1976</th>
<th>Δ</th>
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<tbody>
<tr>
<td>United States</td>
<td>73.1</td>
<td>77.0</td>
<td>6.7</td>
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<tr>
<td>Alabama</td>
<td>77.1</td>
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<tr>
<td>Florida</td>
<td>81.5</td>
<td>86.9</td>
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<td>79.8</td>
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<td>83.6</td>
<td>83.0</td>
<td>-0.6</td>
</tr>
<tr>
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<td>75.2</td>
<td>77.1</td>
<td>1.9</td>
</tr>
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<td>71.1</td>
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</tr>
</tbody>
</table>

*Excluding the self employed and government workers.

SOURCE: U.S. Department of Commerce, County Business Patterns.

of the region's states that small establishments are less important than in
the nation or are shrinking in importance. (Within a given line of business
employment size is related closely to the size of sales.)

In both the nation and the region over three-quarters of all
establishments employ fewer than 10 people, and only .3 percent employ over
500 people. In 1976, 28 percent of private, nonprofessional and nonsupervisory,
employment in Region IV was in establishments employing fewer than 20 employees.

For the nation this figure was 26 percent. Small establishments, of course,
will account for a much smaller share of total employment and sales than
establishments, and the former are the more significant measures of importance.

Data gathered by David L. Birch, who is with the M.I.T. Program on Neighborhood and Regional Change, shows that for both large and small employers in Region IV average sales per establishment are less than in the nation as a whole. The most dramatic difference is in mining. Another difference between the region and the nation is in the age of the average establishment. The average age is less in Region IV. Region IV accounted for a disproportionate share of the nation's new establishments, both large and small, between 1969 and 1976. In light of the region's above average growth rate of income and population, this is not surprising.

Region IV is a part of the Sun Belt, and some of the rest of the country fears that the Sun Belt is attracting too many of its industries. Over the 1969 to 1976 period Region IV did gain a good many more establishments than it lost via migration. Yet, two of the region's states, Alabama and Kentucky, recorded a net loss of establishments during the latter part of this period. The vast majority of the firms migrating into the region during this period employed less than 500 workers in the establishments they set up in the region. Only Alabama, Georgia, and North Carolina appear to have gained establishments employing more than 500 workers. All of these were engaged in manufacturing. Both in- and out-migration was centered in manufacturing, wholesale trade, and retail trade. The relative importance of different industries in gains and losses varied noticeably between the region's states.

Small business engaged in manufacturing and contract construction are more important in Region IV than in the nation, and employment in them and in establishments providing services is growing more rapidly than in the nation. Agriculture is a bit more important employer than in the nation, but it is one
of only two regional industries whose share of national employment is shrinking. (The other one is transportation and other public industry. The shrinkage is minute.) The difference between the regional and national importance of agriculture is slight, and in some of the region's states agricultural employment is less important than in the nation.

For the very small enterprise the sole proprietorship form of organization is the most common. Because of their handicap in obtaining funds, sole proprietorships seldom grow very big, and no major firm can adopt this form of organization. If a huge amount of capital is needed, the corporate form of organization is necessary. The Internal Revenue Service publishes data on receipts and profits per sole proprietorship and per partnership on a state basis. (Note that this is firm data covering all sizes of firms rather than establishment data like the previously mentioned employment data.)

The IRS does not publish like data for small corporations. Forty-nine percent of the firms answering a recent nationwide survey by the National Federation of Independent Business (NFIB) were corporations. Eighty-three percent of those with quarterly sales of $1,500,000 or more were corporations. Seventy-six percent of the firms answering the NFIB survey which had sales of less than $50,000 per quarter were proprietorships. Only 15 percent of the firms replying to the survey had sales of $1,500,000 or more per quarter. Only nine percent had 40 or more employees. Clearly, unless you are concerned only with very small firms, you badly need data on corporations.

Sole proprietorships engaged in agricultural pursuits are relatively more numerous in the region than in the nation. (Included in this category are farming, forestry, and fishing.) Sole proprietorships not engaged in agricultural pursuits, however, are relatively less numerous than in the nation. Thus, it is due to the agricultural firms that sole proprietorships are relatively more numerous in the region than in the nation.
Receipts per firm are less for agricultural proprietorships in the region than in the nation. The reverse is true for nonagricultural firms. In both cases, however, profits relative to sales are below the national average. (There is no data available to indicate what the relationship of profits to investment is.) Both the receipts and profits of the much less numerous partnerships are much smaller in the region than in the nation. In the case of both forms of organization those engaged in agricultural pursuits fare the worst when compared with national figures. The region also fares very badly in mining. Note that the region's poorest performers, agriculture and mining, are industries tied to geography.

3. THE PROBLEM WITH USING AVERAGES FOR A PROFILE

You might consider a group of men as being "normal" or "typical" if you are told that their average height is 5 feet, 10 inches, and their average weight is 150 pounds. Yet, it might be the case that half the group is over 6 feet tall and the other half under 5 feet, 8 inches. No one in the taller group might weigh less than 180 pounds, and no one in the shorter group might weigh more than 130 pounds. Thus, this is hardly a typical group of men. What this example illustrates is that the arithmetic mean may be a very inadequate way to describe a group.

Arithmetic means are not a very useful way to describe the small businesses of Region IV, as the component states are not exceedingly homogenous. Florida, for example, which is the most urbanized state in the region, had 86 percent of its population living in metropolitan areas in 1976. Mississippi, the poorest and least urbanized state in the region, had less than 27 percent of its citizens residing in metropolitan areas in that same year. Florida, the region's wealthiest state, had better than 156 people per square mile. Mississippi had a bit over 50. Agriculture employs relatively and absolutely
more people in Florida than in Mississippi. (See Table 2.) Manufacturing is much more important in Mississippi than in Florida.

Comparing the region with the nation can often produce misleading conclusions. For example, between 1974 and 1975 the profits of nonagricultural proprietorships in the nation and the region declined by the same amount; yet, in Alabama and Tennessee profits rose between these years. Profits for all sole proprietorships declined by 4 percent in the region and 3 percent in the nation, but all the region's states except Florida, Georgia, and Kentucky experienced rising nonagricultural profits. Clearly, business-cycle response differs between the region's states.

Considering only the relative size of different industries in each state can be just as misleading as looking at average figures. For example, manufacturing in Florida is relatively much less important than in the rest of the region and the nation, but more workers in Florida are employed in manufacturing than in Mississippi, which employs more than twice as large a share of its workers in manufacturing. The population of North Carolina is much smaller than that of Florida, but the relative share of its workers employed in manufacturing is so much larger than in Florida that its manufacturing employment dwarfs that of the Sunshine State.

4. STRUCTURAL DIFFERENCES WITHIN THE REGION

In highly urbanized Florida, agricultural employment is more than twice as important as it is in the nation as a whole. In contrast, in Mississippi only one and a quarter times as large a share of total employment is accounted for by agricultural pursuits. Although Florida and Mississippi differ in so many ways, they are the only two states in the region where agricultural employment is relatively greater than in the nation as a whole. Large scale agriculture is much more important in Mississippi than it is in the nation.
Table 2

PERCENT TOTAL EMPLOYMENT BY SIC,*
NATION AND REGION IV
1976

<table>
<thead>
<tr>
<th></th>
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<th></th>
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<td>.4</td>
<td>.4</td>
<td>1.0</td>
<td>.3</td>
<td>.4</td>
<td>.5</td>
<td>.3</td>
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<td>and fisheries</td>
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<td></td>
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<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Mining</td>
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<td>1.2</td>
<td>.3</td>
<td>.5</td>
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<td>.2</td>
<td>.2</td>
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<td>Contract construction</td>
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<td>7.4</td>
<td>5.8</td>
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<td>5.9</td>
<td>6.2</td>
<td>9.2</td>
<td>5.8</td>
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<tr>
<td>Manufacturing</td>
<td>30.3</td>
<td>36.3</td>
<td>15.6</td>
<td>33.1</td>
<td>32.3</td>
<td>39.6</td>
<td>44.1</td>
<td>45.2</td>
<td>38.4</td>
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<td>Transportation and other</td>
<td>6.3</td>
<td>6.0</td>
<td>7.3</td>
<td>7.1</td>
<td>5.3</td>
<td>5.5</td>
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<tr>
<td>Wholesale trade</td>
<td>7.1</td>
<td>6.8</td>
<td>6.9</td>
<td>8.5</td>
<td>6.7</td>
<td>6.6</td>
<td>6.4</td>
<td>5.1</td>
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<td>20.2</td>
<td>19.2</td>
<td>26.0</td>
<td>20.1</td>
<td>20.7</td>
<td>19.1</td>
<td>17.4</td>
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<td>8.9</td>
<td>6.8</td>
<td>5.2</td>
<td>5.2</td>
<td>5.1</td>
<td>4.9</td>
<td>5.5</td>
</tr>
<tr>
<td>real estate</td>
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<td></td>
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<tr>
<td>Services</td>
<td>21.3</td>
<td>16.7</td>
<td>26.2</td>
<td>17.6</td>
<td>18.5</td>
<td>16.3</td>
<td>14.6</td>
<td>13.6</td>
<td>17.9</td>
</tr>
</tbody>
</table>

*Standard Industrial Classification (used by the federal government in data presentation).

Source: U.S. Department of Commerce, County Business Patterns.

Like the nation, only a very small percentage of agricultural establishments in Florida employ more than 500 workers.

While manufacturing is a much larger employer in Region IV than in the nation as a whole, manufacturing employment in Florida is half as important as it is in the nation. The most highly manufacturing-oriented states in the region are the Carolinas. See Table 2. Manufacturing employment has been
shifting southward for many years, and one result of this process has been the concentration of the textile industry in the Piedmont region, particularly that portion of this region in the Carolinas. Increased employment in manufacturing will, of course, lead to subsequent increases in other, supporting industries. In contrast, the expansion of industries serving tourists does little to promote manufacturing employment. Florida, of course, is the prime regional example of a state gaining employment via the tourist trade. Due largely to its high fuel costs and hardly central location, Florida isn't as appealing to manufacturing as are the Carolinas.

Like Florida, Kentucky stands out from the rest of the region because of its atypical employment structure. With the exception of Kentucky and Alabama, the region's states are much less dependent on mining employment than is the nation. Mining is much more important in Kentucky than in Alabama. Kentucky employs 3.5 times as many people, relatively, in mining than does the nation. Eighty-five percent of those employed in Kentucky mines are engaged in extracting coal, and 87.6 percent of these miners work for establishments employing 500 or fewer workers. In the nation, only 78.6 percent of mining equipment is in these smaller establishments. The underground coal mining which dominates mining in Kentucky, but not the nation, is characterized by a lot of what might be called "mom and pop" operations.

The objective of mining operations differs significantly from state to state. In Georgia the major extractive industry is kaolin. In Florida phosphate is the major extractive industry. Alabama is blessed with iron ore, limestone, and coal; thus, Birmingham is a steel town. Birmingham is also a medical center, but this is not the result of its natural endowments. It has become a medical center because of a choice made by the state government, which has put a good deal of money in a medical school there. In contrast,
Atlanta is a medical center largely because of a private medical school greatly helped by Coca-Cola profits and its central location. (Medical organizations are usually sole proprietorships or partnerships, particularly the former.)

In Region IV transportation and other public utilities (a federal Standard Industrial Classification) employs somewhat fewer people, relatively, than does the nation. Small firms accounted for more of the employment growth in this industry nationally than in the region between 1970 and 1976. In Florida and Georgia this industry employs relatively more people than in the nation. These two states also stand out from the nation in that small establishments are least important in transportation and other public utilities in them, but in the nation small establishments are least important in manufacturing. A variety of factors probably play a part in accounting for both the greater importance of transportation and other public utilities and the larger average-sized establishments in Florida and Georgia. Georgia is the distribution center for the Southeast and has the nation's second busiest airport. (Its new airport will be the largest in the nation.) Most of the travel between the U.S. and Latin America takes place via Florida. The business with Latin America is large and increasing rapidly. Florida is much larger than the other states in the region and is growing much faster. Georgia is just nosed out by North Carolina for second place in terms of population. Tourism is the major industry in Florida, and most of the travelers to Florida are funneled through Georgia. Goods, too, largely reach Florida via Georgia. The nation's largest electric utility holding company is based in Georgia, where its largest component is based. Georgia is also headquarters for a regional telephone company and a number of trucking companies.
Region IV employs relatively fewer people in wholesale and retail trade than does the nation, but Florida employs relatively more than does the nation. Georgia, with one of the nation's major convention cities, Atlanta, virtually matches the national proportion of employment in retailing. See Table 2.

Georgia and Tennessee employ relatively more people in wholesaling than does the nation as a whole. Georgia employs 20 percent more; Tennessee 10 percent more. Clearly Florida retailers have more out-of-state customers to tap than do the other states in the region. Georgia retailers benefit from Florida-bound tourists, and the state is a regional wholesaler because of its central location and the convergence of transportation links in Atlanta. Tennessee has long served as a linkage point for trade between the Southeast and Midwest because of its border location and access to the Mississippi River. Since small establishments are very numerous in wholesaling and retailing; thus, strength here boosts the importance of small businesses.

Florida is the only state in the region where services are a more important employer than in the nation as a whole. Tennessee has the lowest relative employment in services within the region. Tourism certainly plays a major role in the unusual importance of services in Florida. In Florida, 3.95 percent of those other than the self-employed or those working for the government are employed in hotels and other lodging places. For the nation this figure is 1.42 percent. Auto services, which are also influenced by tourism, also account for relatively more employment in Florida than in the nation. Small firms are exceedingly common in services.

David L. Birch of M.I.T. (mentioned earlier) conducted some research which revealed a factor which may affect the growth of employment in services in the South. He discovered that in manufacturing the great majority of jobs generated in the South are controlled in the Northeast and North Central
sections of the country. Entrepreneurial southerners are, he says, "latching on to the growing service sector and are aggressively dominating the generation of jobs in this sector throughout the country." Certainly greater opportunities in services for southerners could be a factor in the much more rapid job growth in this sector in the South than in the nation.

5. THE IMPORTANCE OF SMALL ESTABLISHMENTS

The relative importance of large and small employers varies among the 9 Standard Industrial Classifications seen in Table 2. In several of the region's states, agriculture, mining, contract construction, and wholesale and retail trade have significantly higher employment shares for small businesses than do the other classifications.

In South Carolina only half of manufacturing employment in 1976 was in establishments employing 500 or fewer workers. At the other extreme, in Florida over 70 percent were in establishments employing 500 or fewer workers. For the nation this percent has 58.3 percent. In Georgia, Kentucky, North Carolina, and Tennessee, all agricultural employment is in establishments employing 500 or fewer people. In all the region's states over 90 percent of employment in wholesale and retail trade is in establishments employing 500 or fewer workers.

There appears to be a good deal of interstate variance between the relative importance of small employers in Region IV. Some of this variance is due to differences in the nature of the work done by most of the establishments involved. For example, the Mississippi Delta offers farmers drastically different conditions than do the Appalachian mountains. Underground coal mining differs significantly from phosphate mining. Running a hotel differs from running a hospital. Steel making differs radically from apparel manufacturing. In short, economies of scale differ drastically between industries, and the region's states specialize in different industries.
Large establishments arise where there are substantial economies of scale and a market reachable at a reasonable cost which is large enough to absorb the high level of output of the more capital intensive facilities required to obtain great economies of scale. Manufacturing offers far more economies of scale than does contract construction, retailing, finance, and so forth. Observe that small establishments are relatively more important in the industries with the least economies of scale, such as finance, real estate, and services. Farms are larger in the Mississippi Delta where more mechanization and, therefore, economies of scale are obtainable than in, say East Tennessee or Kentucky.

The relative importance of small establishments is also related to the average age of these establishments, as businesses normally start small and, if they survive, which most don't, grow. Nearly half of the new business incorporations in the region in 1977 were in Florida. See Table 3. This appears to be both a product of Florida's larger population and more rapid growth rate. An examination of population figures and growth rates for the region suggests that population size is the more important factor in promoting new incorporations. The level of per capita income appears to play a lesser role than population size. Florida's exceptionally large share of new business incorporations is certainly related to the fact that both population and per capita income are larger and growing more rapidly than in the other states in the region. The huge flow of visitors is also a major factor. (Georgia has the second highest level of per capita income in the region. Kentucky and Tennessee tie for third place.) A state whose natural advantages can, for the most part, only be exploited by firms utilizing a heavy investment of funds will lag in new incorporations, since relatively few people can obtain enough funds to start such a business. Clearly, Florida is not such a state.
### Table 3

**POPULATION AND NEW BUSINESS INCORPORATIONS**

**REGION IV, 1977**

<table>
<thead>
<tr>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>7</td>
<td>10</td>
</tr>
<tr>
<td>Florida</td>
<td>24</td>
<td>24</td>
</tr>
<tr>
<td>Georgia</td>
<td>10</td>
<td>14</td>
</tr>
<tr>
<td>Kentucky</td>
<td>5</td>
<td>10</td>
</tr>
<tr>
<td>Mississippi</td>
<td>8</td>
<td>7</td>
</tr>
<tr>
<td>North Carolina</td>
<td>9</td>
<td>16</td>
</tr>
<tr>
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<td>11</td>
<td>8</td>
</tr>
<tr>
<td>Tennessee</td>
<td>10</td>
<td>12</td>
</tr>
</tbody>
</table>


Retailing dominated employment growth in small firms between 1970 and 1976 in both the region and the nation. The most striking difference in the composition of employment growth among small firms was the role of services and manufacturing, which followed retailing as the next most rapidly growing sectors in the region, but which trailed half or more of the 9 Standard Industrial Classifications in the nation. The growth of retailing in the nation, where it accounted for more than half of the employment growth in small establishments, was far more important than in the region. Yet, the region's share of the nation's employment in retailing grew in spite of the fact that retailing accounted for a much smaller portion of employment growth.
in the region than it did in the nation.

Only in agricultural pursuits, contract construction, and manufacturing does the region have a larger share of workers in small establishments than it has of the nation's population. Total employment in establishments of all sizes, excluding the self-employed and government workers, represents a smaller share of national employment than the region's share of national population. Small establishments come closer to matching the region's population share than does business as a whole. (A relatively larger number of housewives and children lower the percent of the population employed.)

6. PROFITABILITY AS MEASURED BY PROFITS TO RECEIPTS

Partnerships are relatively few in number, and a rather large number of those in the region lose money. (One suspects that sometimes partners' objective isn't profits: it's tax losses to cover income generated outside the partnership.) The region's partnerships' profitability, as measured by profits to receipts, is drastically below the nation's. This form of organization is most common in agriculture and services, both nonprofessional and professional. Real estate investors also often choose to form a partnership.

Sole proprietorships in the region and the nation responded similarly to the business cycle in 1974 and 1975. If we exclude agricultural proprietorships, regional and national firms shared the same experience: a 1.7 percent decline. Yet, while the region as a whole closely paralleled the national experience, this was not true for each of the region's eight states.

Alabama and Tennessee sole proprietorships enjoyed a rise in profits from 1974 to 1975. Alabama's gain was significant. Most of Alabama's gain was explained by a 56 percent reduction in agricultural losses and a substantial gain in construction, insurance, and services, mainly medical and
health services, whose gain accounted for 42 percent of the 1974-1975 gain in nonagricultural profits. Over the 1970-1976 period, health services in Alabama grew enormously. Tennessee experienced a like-sized gain in this area. Due to gains in bituminous coal, mining in Tennessee grew tremendously over this period.

Florida, Georgia, Kentucky, and South Carolina, in contrast to the other states in the region, experienced reductions in nonagricultural profits from 1974 to 1975. By far the largest profit reduction was suffered by South Carolina, whose profits declined by 12 percent. Construction, which experienced an enormous employment gain from 1970 to 1976, accounted for a large share of the profit decline in South Carolina.

The most significant shared profit loss in the region was in livestock. Only North Carolina escaped a livestock loss in 1975. Many of the region's states experienced crop losses. The nation lost money on livestock, but not on crops. Florida suffered a $103,638,000 livestock loss. This was the largest livestock loss in the region.

Region IV sole proprietorships are relatively unprofitable. They accounted for over 16 percent of the nation's sole proprietorship receipts in 1975, but they accounted for only a bit more than 12 percent of profits. Since 14 percent of the nation's income was received by the region's residents, sole proprietorships were not assisting in the long-term rise of regional per capita income relative to the national average.

Nonagricultural sole proprietorships did a bit better than did those in agriculture. They accounted for 14.2 percent of this form of organization's total profits in 1975.

A below average performance of farming is certainly not unprecedented. Historically farming has been relatively large in the region and, at least since
the War Between the States, less profitable than in the nation. However, in 1975 receipts from agriculture accounted for 20.4 percent of sole proprietorship receipts in the nation and only 18.5 percent in the region. Thus, as an income source, agriculture today is relatively less important in the region than in the nation, a situation justified by its lower profitability, assuming that investment per farm is not proportionally lower in the region than in the nation. (There is data which indicates that average investment per farm is less in the South than in the rest of the nation.)

Average receipts per proprietorship in the Standard Industrial Classification agriculture, forestry, and fishing were $20,578 for the nation in 1975 and only $13,972 in the region. Forestry is relatively important in the region, but fishing is not very significant even in some of the coastal states.

The lower profitability of the average Region IV sole proprietorship is partially a result of lower receipts per firm in some lines of business and is partially the product of industrial structures differing from the nation's. Size, as measured by receipts, appears to explain the lower earning power of some industries in Region IV, as Internal Revenue Service data shows that, on the average, as firm size rises, so does the ratio of profits to receipts. Profitability differs, of course, between industries.

The profits and receipts of the average sole proprietorship in Georgia and the nation shown in Table 4 illustrate the regional and national profit differences by industry. (Profits in Georgia manufacturing were 13 percent of receipts; while in wholesale and retail trade they were only 5.3 percent. Investment was almost certainly higher in manufacturing.

If Georgia firms in each industry had earned profits equal to those earned nationally, Georgia's total sole proprietorship profit would have been
Table 4
GEORGIA AND THE U.S.
SOLE PROPRIETORSHIP RECEIPTS AND PROFITS
1975

<table>
<thead>
<tr>
<th>Industry</th>
<th>Average Profit U.S.</th>
<th>Average Profit Georgia</th>
<th>Average Receipts U.S.</th>
<th>Average Receipts Georgia</th>
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</thead>
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<tr>
<td>Agriculture, forestry, and fishing</td>
<td>$1,659</td>
<td>$132</td>
<td>$20,578</td>
<td>$15,094</td>
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<tr>
<td>Mining</td>
<td>5,091 (13,351)</td>
<td>63,499 NA</td>
<td>34,758</td>
<td>34,306</td>
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<tr>
<td>Construction</td>
<td>4,919</td>
<td>3,880</td>
<td>39,156</td>
<td>60,905</td>
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<tr>
<td>Manufacturing</td>
<td>4,693</td>
<td>7,928</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Transportation, communication, electric, gas</td>
<td>3,549</td>
<td>1,754</td>
<td>28,174</td>
<td>15,649</td>
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<tr>
<td>and sanitary service</td>
<td></td>
<td></td>
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</tr>
<tr>
<td>Wholesale and retail trade</td>
<td>4,495</td>
<td>3,919</td>
<td>67,630</td>
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<td>Finance, insurance, and real estate</td>
<td>5,057</td>
<td>4,441</td>
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<td>16,990</td>
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<tr>
<td>Services</td>
<td>6,060</td>
<td>6,277</td>
<td>18,456</td>
<td>21,519</td>
</tr>
</tbody>
</table>

Source: Internal Revenue Service.

nearly 23 percent greater, and this profit would have equaled 2 percent of the nation's larger profit from sole proprietorships rather than the 1.6 percent actually achieved. (In 1975 Georgia had 2.3 percent of the nation's population and 2.0 percent of its income.) Computing Georgia's profits, assuming that each of its industries had the same relative size as in the nation, would not produce anywhere near this much improvement. Therefore, the major problem is the relatively low profits per firm rather than too
large a share of firms being in low-profit industries.

7. CONCLUSION

Data is not adequate to obtain an economic profile of small business in Region IV which is complete or in which one can have a high degree of confidence. Investors are more interested in the return on investment figure, which is not available, than a ratio of profit to receipts. Internal Revenue Service data on sole proprietorships and partnerships is not broken down by firm size. The IRS does not provide small business corporate data on a state basis. Department of Commerce data is available only on an establishment basis, and receipts are not broken down by employment size or number of establishments. When only one or a few establishments make up a classification, to protect them, no figures are given for this class.

Department of Commerce data cannot be correlated with Internal Revenue Service data.

Despite the paucity and incompleteness of the data, it seems highly unlikely that small businesses in Region IV are actually much less common in the region than in the nation and are much more profitable, or that small farms are springing up like toadstools after a heavy rain. Differences in industrial structure, at least in broad outline, as revealed in available data are compatible with what one familiar with these states would observe.

Variances between the region's states are great enough so that it appears unwise to use the region as a basis for making decisions. Some of the states' small businesses are mirrored better by national averages than those of another regional state. Georgia's industrial structure, for example, is much more like the nation's than Florida's. Manufacturing is more important in the region than in the nation. In Florida manufacturing is less important than in the nation.
1. INTRODUCTION

The diversity, dynamism, and constant change in American business are pervasive themes in academic and professional publications as well as in the popular media. Businesses differ with respect to management techniques and philosophy, and to goals, organization, size, governance, and financial arrangement. Each business, whether old or new, large or small, or production or service oriented, faces the problem of finding persons skilled in the management arts who are capable of providing leadership toward meeting company goals within the contemporary business and economic climate. Controversial issues in governmental regulations, demands by workers for increased roles in significant areas of decision making, maintenance of satisfactory profits, and in employee wage and work agreements are only a few of the many complex problems that are associated with the management of business firms.

Although much has already been written and said about the management and financial problems facing businesses, only recently has attention been focused so decisively on persons responsible for resolving those problems, namely, business managers. A careful search of the literature shows that most of the studies available have dealt with the managers of large businesses and that relatively little is known of the persons who head the nation's small businesses; furthermore, there is a veritable paucity of data about women, the aged, and people from minority groups who fill those positions. Since small businesses are one of the main reasons for the economic strength of this nation, it is important that the people
who run these businesses be understood. If the number of small businesses is to grow, the women, aged, and minorities of America must have more "equality of opportunity" and must play a greater role. An understanding of the motivations, ideologies, and goals of small business owners could lead to greater future participation by these three groups.

Information about owners and managers of small businesses from these groups regarding their orientation, social origins, career patterns, geographical movement, occupational and educational backgrounds, and personalities has come primarily from their statements and writings. The material available provides some insight but is quite limited in perspective and in some cases is based more on speculation than on hard fact. Although there have been several investigations of females, the aged, and minority persons who are leaders in large businesses, few studies of subtle perception have been directed specifically toward uncovering knowledge about the careers of people from these groups in small businesses.

In sum, there has been no systematic and accurate career profiles of female small business owners and managers, or for the elderly and persons from minority groups. And we know little of how those individuals compare among regions. Further, the informational gap is not being closed at a desirable rate.

Purpose of the Study

The primary purpose of this study was to characterize females, elderly persons, and persons from minority groups who own or manage small businesses in the South; this purpose was achieved through an investigation of their social origins, educational background, career routes, and other relevant information. More specifically, the study was designed to produce: (1) an accurate analysis of the vertical occupational mobility, career paths,
and social background--family, birth, and geographic origin--of these groups; (2) limited cross-comparisons of these business executives between states and types of businesses; and (3) a contrast of these business persons with their typical white male small business counterparts.

A number of questions were asked of the referenced groups to support the primary purpose of the investigation. Who are the people from these groups who have risen to top positions in the Mid-South area? Is there an interdependence of social, spatial, and occupational mobility in their backgrounds that can be documented? What avenues of career mobility did most follow? Are such persons found most often in one kind of business or in one state? What are their ages, family compositions, military records, and birthplaces, and what is the commonality of their parentage and ancestry?

Where were these outstanding business leaders educated, and what factors or developments pointed them to an ultimate career in business? What other alternatives were available? Are there profound differences between female business leaders and male business leaders? between black leaders and white leaders? or between the aged small business owner or manager and younger business leaders?

Theoretical Framework

The universe in this study was comprised of all of the small businesses in Mississippi, Georgia, Kentucky, Tennessee, Florida, South Carolina, North Carolina, and Alabama. A sample of approximately 1,000 small business owners and managers formed the informational base for the study. The primary source for names of persons in the universe who own businesses or occupy managerial positions, and who were included in the research design, was the Small Business Administration, Business and Professional Women's clubs, black
business organizations, SCORE chapters, and the directories of manufacturing and retailing for the respective states. This methodology allowed for enough responses from different types and sizes of firms throughout the region so that comparisons could be drawn, analyses made, and patterns discerned (with one exception which will be noted later). Personal visits were made in some cases to gather information from data sources.

Method of Data Collection

A questionnaire survey was conducted to collect necessary data about the relevant owners' or managers' careers. A research instrument first used by W. Lloyd Warner (7) for business and government executives and later refined and used by Michael Ferrari for American College presidents (2) was modified to apply more directly to female, elderly, and minority executives. Many questions were kept virtually intact to facilitate comparisons within and between groups and with findings or previous studies. The research instrument was pilot tested with a sample of owners and managers before it was implemented. The questionnaire contained a few open-ended questions to promote greater candor about the conscious motivations and ideologies that the respondents felt played important roles in their career patterns.

Personal interviews were conducted with the respondents where appropriate and necessary. The interviews helped to clarify views and to gain greater insight into the particular problems he or she has faced in a world dominated by white males. Also, questioning in the personal interviews helped to determine what motivated these leaders to pursue careers in business; that is, what value or situations guided them to their basic career paths.

The questionnaire obviously provided an expanse of data and information, much of which cannot be included in a short article for a regional volume. The material is expected to be incorporated in a book or monograph that is much more complete. Future plans include compiling and analyzing this kind of material from a sample of owners and managers nationwide into a comprehensive volume.
2. WOMEN

Because the American socialization process has traditionally emphasized independence, work, and career orientation for males, and dependency and passivity for women, the number of female small business owners has been small. The women's liberation movement, however, is changing this orientation, albeit slowly. Although feminists have often alleged that prejudice was the reason that women are found so rarely in business, previous studies have pointed out that the socialization process has tended to keep women from going into business.

Because she lacks conviction of her own ability, she tends to undermine her own self-confidence. Because she fails to expose herself, she develops a pattern of avoidance of risk taking. Because her motivation is other-directed, she fails to set goals for herself and plan how to achieve them. The result is low achievement motivation. Because she fails to set goals and plans, she doesn't seek and she doesn't prepare. Because she doesn't set goals, plans, seek, prepare, she doesn't achieve. Lack of achievement helps to contribute to her own feeling of inferiority and leads her right back to where she started--dependent, passive and ambivalent. (1)

More and more women are becoming involved in business management. Women who want a career in small business today do not necessarily fit a single mold. Changing attitudes toward marriage and family life are affecting women's role in small business. Increased divorce rates have resulted in many women becoming responsible for their own financial support. Also, economic pressures brought about by inflation and the desire for a high standard of living mean that a second income is a necessity in most American families. All of these factors are contributing to women's growing interest in small business careers.

Unlike some other groups, women small business owners and managers were, on the whole, greatly influenced by their husbands and families in
their choices. Such statements as the following were common.

My husband had a very great influence on my career; had I not been married to a man who wanted me to be a successful professional, I would not have been able to venture out on my own, either emotionally, or financially.

I must say my husband has had a great part in helping. Although he does not help in either of the businesses, he understands my work and provides a good shoulder to lean on.

My husband always encouraged me in my work and never complained about the inconveniences it caused.

My husband wanted me to take this business because he knew that I liked this kind of work. He helped me very much in the business.

My spouse has always encouraged me to do something along the lines of my present career. My association with his business dealings overcame some of my feelings about a career. Having been raised in a very traditional Southern environment (with home and motherhood my main objectives), I had a lot to overcome.

Such comments as the above were expressed by 90 percent of the female respondents. This was in stark contrast to the male respondents who generally stated that no one had influenced their choice of career. In fact, it was almost possible to determine the sex of a respondent simply by the answer to the question on whether there was any family influence. Although other family members were occasionally mentioned, it was the husband that generally received credit for the small business career. Even divorcees gave their ex-husbands credit in many cases. One unmarried respondent even replied, "My concubine had total influence on the current business career."

As to why they went into business for themselves, the typical response mentioned children (the average woman has 2.3 children). For example:

My spouse approved of my occupation as a hair-dresser but encouraged me to own and operate my own business with his help and assistance. But the main reason, aside from enjoying the work, I could continue to
carry on my business at, or nearby, home, so I was available to my children as they grew up.

I chose my career because of the ease of adjusting a schedule to accommodate having a family and caring for the children.

My reason for going into my own business is a simple one. I am the mother of five school aged children. My business permits me to arrange my work schedule to provide maximum time with the children.

In most respects, women small business owners are similar to the typical small business owner—the white male. The woman is a little younger, 42.6 years versus 46.4 for white men. She is about four years younger than the average male and also began her work career four years later than the male (19.8 years versus 15.7). She assumed her present position when she was 35 years old, the same as the male.

The most glaring difference between women and men was marital status. Only 76.5 percent of the women were married while 97.3 percent of the men had a spouse. Ten percent of the women were divorced and 5.9 percent were widowed.

The average number of previous managerial positions held by women owners was 1.1. White males had held 1.94 managerial positions before going into business for themselves.

Table 1 summarizes the educational background of female and white male small business owners.

Thus, the woman small business owner has less education than the male, but those with some college background have more often majored in business. In addition, a higher percentage of women have graduate degrees.

Table 2 summarizes the type of position both women and men obtained in their first full time job. The most obvious differences is that men generally worked as unskilled, or semi-skilled laborers, while women were working in clerical or sales positions or as school teachers.
Table 1
EDUCATIONAL BACKGROUND

<table>
<thead>
<tr>
<th></th>
<th>Women</th>
<th>White Men</th>
</tr>
</thead>
<tbody>
<tr>
<td>% Having Attended College</td>
<td>76.5%</td>
<td>96.4%</td>
</tr>
<tr>
<td>% of Above Majoring in Business</td>
<td>57.9%</td>
<td>30.8%</td>
</tr>
<tr>
<td>% With at Least a Bachelors Degree</td>
<td>45.1%</td>
<td>71.5%</td>
</tr>
<tr>
<td>% With Graduate Degree</td>
<td>13.7%</td>
<td>4.8%</td>
</tr>
</tbody>
</table>

Table 2
FIRST FULL TIME POSITION

<table>
<thead>
<tr>
<th></th>
<th>Women</th>
<th>White Men</th>
<th>Minority</th>
<th>Aged</th>
</tr>
</thead>
<tbody>
<tr>
<td>Worker - unskilled or semi-skilled</td>
<td>8.2</td>
<td>46.2</td>
<td>22.2</td>
<td>27.3</td>
</tr>
<tr>
<td>Worker - skilled, mechanic</td>
<td>4.1</td>
<td>10.3</td>
<td>7.4</td>
<td>18.2</td>
</tr>
<tr>
<td>Clerical worker, salesman</td>
<td>36.7</td>
<td>12.8</td>
<td>14.8</td>
<td>36.4</td>
</tr>
<tr>
<td>Minor executive, foreman</td>
<td>2.0</td>
<td>5.1</td>
<td>3.7</td>
<td>-0-</td>
</tr>
<tr>
<td>Major business executive</td>
<td>-0-</td>
<td>2.6</td>
<td>-0-</td>
<td>-0-</td>
</tr>
<tr>
<td>Owner small business</td>
<td>10.2</td>
<td>7.7</td>
<td>11.1</td>
<td>-0-</td>
</tr>
<tr>
<td>School teacher</td>
<td>10.2</td>
<td>-0-</td>
<td>7.4</td>
<td>9.1</td>
</tr>
<tr>
<td>College faculty</td>
<td>-0-</td>
<td>2.6</td>
<td>3.7</td>
<td>-0-</td>
</tr>
<tr>
<td>Other</td>
<td>20.4</td>
<td>7.7</td>
<td>11.1</td>
<td>-0-</td>
</tr>
<tr>
<td>Government</td>
<td>6.1</td>
<td>2.5</td>
<td>-0-</td>
<td>9.1</td>
</tr>
<tr>
<td>Military</td>
<td>2.1</td>
<td>2.5</td>
<td>14.8</td>
<td>-0-</td>
</tr>
<tr>
<td>Farming or Ranching</td>
<td>-0-</td>
<td>-0-</td>
<td>3.7</td>
<td>-0-</td>
</tr>
</tbody>
</table>

100.0   100.0   100.0   100.0
Table 3 is similar to Table 2 except that it summarizes the primary occupation of the father of the small business owner. All four categories of owners (white males, females, minority ethnic groups, and the aged) are included in Table 3. There appears to be little difference in the backgrounds of the women's fathers as compared to those of the men.

Table 4 summarizes the educational level of the parents of small business owners. The parents of women owners are slightly more highly educated than the parents of the male owners.

Most women small business owners were born in the United States, as were their spouses and parents. The figure for all categories was 98 percent or higher. The percentages for the males were nearly identical.

The typical woman owner was born in a small town, as is shown in Table 5. The males were even more small town oriented than were the women. Nearly three-fourths of the women were born in the eight state southeastern region covered by this study. Just over three-fourths of the males were born in the region.

The statistics show that the typical small business woman is slightly younger than the male, is more apt to be unmarried, more likely to have had clerical, sales, or teaching experience, and has had slightly less managerial experience before assuming her present position. Her husband has probably been very instrumental in her decision to start a small business. One of the most common motivating factors was the desire to have time available when needed by family members, particularly children.

One woman respondent, in answer to the question regarding why she had chosen a small business career, gave a reply that aptly sums up this section of this article:
## Table 3

**OCCUPATION OF FATHER**

<table>
<thead>
<tr>
<th>Occupation</th>
<th>Women</th>
<th>White Men</th>
<th>Minority</th>
<th>Aged</th>
</tr>
</thead>
<tbody>
<tr>
<td>Worker -unskilled or semi-skilled</td>
<td>20.0</td>
<td>17.9</td>
<td>39.4</td>
<td>25.0</td>
</tr>
<tr>
<td>Worker -skilled</td>
<td>16.0</td>
<td>15.4</td>
<td>24.2</td>
<td>8.3</td>
</tr>
<tr>
<td>Clerical worker or sales</td>
<td>2.0</td>
<td>7.7</td>
<td>8.3</td>
<td></td>
</tr>
<tr>
<td>Foreman, minor executive</td>
<td>10.0</td>
<td>2.6</td>
<td>8.3</td>
<td></td>
</tr>
<tr>
<td>Major business executive</td>
<td>2.0</td>
<td>2.6</td>
<td>3.0</td>
<td></td>
</tr>
<tr>
<td>Owner of a small business</td>
<td>28.0</td>
<td>35.9</td>
<td>6.1</td>
<td>25.0</td>
</tr>
<tr>
<td>School teacher</td>
<td>2.0</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lawyer</td>
<td></td>
<td></td>
<td>3.0</td>
<td></td>
</tr>
<tr>
<td>Engineer</td>
<td>2.0</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>4.0</td>
<td>2.6</td>
<td></td>
<td>8.3</td>
</tr>
<tr>
<td>Government</td>
<td>4.0</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Military</td>
<td>2.0</td>
<td>5.1</td>
<td>3.0</td>
<td></td>
</tr>
<tr>
<td>Farming or Ranching</td>
<td>8.0</td>
<td>10.3</td>
<td>21.2</td>
<td>16.7</td>
</tr>
<tr>
<td></td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>
Table 4
PARENTS' EDUCATIONAL LEVELS

<table>
<thead>
<tr>
<th>FATHER'S EDUCATIONAL LEVEL</th>
<th>Women</th>
<th>White Men</th>
<th>Minorities</th>
<th>Aged</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than high school</td>
<td>23.6</td>
<td>37.5</td>
<td>56.0</td>
<td>58.3</td>
</tr>
<tr>
<td>Some high school</td>
<td>9.8</td>
<td>12.5</td>
<td>20.0</td>
<td>8.3</td>
</tr>
<tr>
<td>High school graduate</td>
<td>31.4</td>
<td>32.5</td>
<td>8.0</td>
<td>33.3</td>
</tr>
<tr>
<td>Some college</td>
<td>17.6</td>
<td>12.5</td>
<td>8.0</td>
<td></td>
</tr>
<tr>
<td>College graduate</td>
<td>13.7</td>
<td>2.5</td>
<td>4.0</td>
<td></td>
</tr>
<tr>
<td>Post graduate</td>
<td>3.9</td>
<td>2.5</td>
<td>4.0</td>
<td></td>
</tr>
<tr>
<td></td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>MOTHER'S EDUCATIONAL LEVEL</th>
<th>Women</th>
<th>White Men</th>
<th>Minorities</th>
<th>Aged</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than high school</td>
<td>21.6</td>
<td>20.0</td>
<td>44.0</td>
<td>41.7</td>
</tr>
<tr>
<td>Some high school</td>
<td>11.8</td>
<td>10.0</td>
<td>20.0</td>
<td>8.3</td>
</tr>
<tr>
<td>High school graduate</td>
<td>29.4</td>
<td>37.5</td>
<td>20.0</td>
<td>16.7</td>
</tr>
<tr>
<td>Some college</td>
<td>19.6</td>
<td>22.5</td>
<td>8.0</td>
<td>16.7</td>
</tr>
<tr>
<td>College graduate</td>
<td>13.7</td>
<td>7.5</td>
<td>4.0</td>
<td>8.3</td>
</tr>
<tr>
<td>Post graduate</td>
<td>3.9</td>
<td>2.5</td>
<td>4.0</td>
<td>8.3</td>
</tr>
<tr>
<td></td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
</tbody>
</table>
### Table 5

**POPULATION OF CITY WHERE BORN**

<table>
<thead>
<tr>
<th>Rural or less than 2500</th>
<th>Women</th>
<th>White Men</th>
<th>Minority</th>
<th>Aged</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>43.1</td>
<td>57.5</td>
<td>33.3</td>
<td>58.3</td>
</tr>
<tr>
<td>2,500 - 10,000</td>
<td>17.6</td>
<td>17.5</td>
<td>20.8</td>
<td>16.7</td>
</tr>
<tr>
<td>10,000 - 15,000</td>
<td>13.7</td>
<td>10.0</td>
<td>4.2</td>
<td>8.3</td>
</tr>
<tr>
<td>15,000 - 100,000</td>
<td>9.8</td>
<td>5.0</td>
<td>20.8</td>
<td>8.3</td>
</tr>
<tr>
<td>Over 100,000</td>
<td>15.7</td>
<td>10.0</td>
<td>20.8</td>
<td>8.3</td>
</tr>
<tr>
<td>Born in Region?</td>
<td>72.5%</td>
<td>78.1</td>
<td>100.0</td>
<td>83.3</td>
</tr>
</tbody>
</table>

Business, especially my own, is the most open, challenging and limitless field for a woman today. The women in business today are really pioneers. Prior to this, women have been considered real exceptions to the rule if they succeeded in business. Today's women are proving that women have a place in business and the professions that is not the exception but the norm. I'm proud to be a part of that effort. Besides all that, I enjoy what I do.

### 3. MINORITY PERSONS

Although minority race individuals make up over 17 percent of the U. S. population, such persons own or manage only about 4 percent of the small business establishments in the nation. This relatively small number of minority owned businesses compares unfavorably with mainstream enterprises with respect to size of receipts, industry distribution, and location. Census figures disclose that minority owned businesses account for only a little more than 2 percent of the gross receipts of the small business sector. With regard to industry, few minority owned businesses are engaged in manufacturing
(only 2 percent of all manufacturers) while a much greater percentage were engaged in personal services (about 13 percent of all such businesses). A high percentage, nearly three-fourths, were located in urban areas with populations in excess of 50,000 population.

Since the percentage of minority owned businesses is so much smaller than the minority percentage of the population, the profile of the minority small business owner is of particular interest. This study showed that most minority small business owners had definite goals that caused them to go into business for themselves. The most often mentioned goal was to have a sense of independence and to be free from outside control. Typical of the feeling of many respondents was the following quotation taken from one of the questionnaires.

The reason for my selection of business career was the greater amount of flexibility and independence over other occupations. The decision making responsibilities, as well as planning, financing and other aspects of business, are a constant challenge.

I prefer being independent.

I wanted to be my own boss and be in a better position to help others.

In addition, these individuals seemed to have a strong sense of enterprise which led them to want a better life for themselves and their families. The consensus was that the best way to achieve this better life was through the ownership of economic resources. Typical comments included the following:

I chose a business career because I wanted to get ahead at an accelerated pace.

I wanted lots of money. When you are on salary you are limited as to the amount of money you can earn.
My own business provides a better chance to move up in the world.

I wanted to give my family a better life and to prove to myself and others that I could succeed.

My family was poor and I grew up in the ghetto. Being poor forced me into wanting a better life for me and my family. At the time I was in school, a business career was the furthest thing from the minds of most blacks. The reason I chose a career in business was because in business one has the opportunity to control his destiny, all things being equal and fair.

The typical minority small business person is slightly younger than the white male or the female business person. The average age for the minority group was 40.4 years compared to 46.4 for white men and 42.6 for women. The average age of the minority respondents when they achieved their present positions was 34.4 years as compared to 35 for white males and women. Thus, the average minority person has been in business only about six years while the white male has operated his own business for eleven years.

Regarding marital status, only 81.8 percent of the minorities were married as compared to 97.3 percent for white males. Most of the unmarrieds were young people who had never been married; there was a very low percentage (3.0 percent) of widowed and divorced owners. Consequently, the difference in marital status may be due solely to the fact that there is a six year difference in the average ages.

Approximately 63 percent of the minority owners had attended college (it was 96.4 percent for white males). A bachelors degree was held by 48.5 percent (71.5 percent for white men) and 15.2 percent held masters degrees (only 4.8 percent for white men). The minority small business owners apparently did not get as high of grades in college as individuals from other
groups as only 14.3 percent of those who attended college were members of honoraries. Among white men who attended college, 27.8 percent were members of honoraries and 43.5 percent of women held the same distinction.

Table 2 compares the first full time position held by each group of owners. The only thing particularly noticeable about minorities is that a higher percentage got their start in the military.

In Table 3, the occupation of the father of the business owners are compared. The most obvious differences between minorities and the other groups is that a much greater percentage of minority fathers were skilled or unskilled workers, or farmers. Only 6.1 percent of the minority fathers owned a small business while the rates for white men and women were 35.9 and 28.0 percent respectively.

Table 4 summarizes the educational levels of parents. The most obvious difference between minorities and other groups is that about three-fourths of the fathers, and nearly as many mothers, have less than high school educations.

The final area where the average minority business person differs from other groups is with respect to location of birth. Whereas Table 5 shows that the other groups were very small town oriented, over 40 percent of the minorities were born in large cities. Also, a greater percentage of the minorities were born in the Southeast as compared to the other groups.

Minority small owners are apparently more similar to minority non-owners than to business owners from the other groups. The minority owners are younger, lesser educated and have poorer family backgrounds, more often from large cities, than other business owners. However, they do have a will to get ahead.
Hopefully, members of minority groups will be able to expand their ownership of small businesses in future years. In addition to increasing the economic development of themselves and the nation as a whole, successful minority small business owners could boost the self-confidence of other minority group members. Visible evidence of minority small business would have a healthy impact on the minority community and could create a feeling among the citizens that they, too, could make it within the system. These successful enterprises are dependent on the effort and enterprise generated by the minority small business owners. The one common trait that permeated the owners in this study was the desire for a better life and the recognition that this desire could only be fulfilled by hard work. The statement expressed by one of the survey respondents aptly summarizes this philosophy: "The more you work, the more you have."

As has been pointed out by others:

The need for extensive management and technical assistance is not unique to minority business, but it is indeed critical to the survival of any small business. However, the health of minority businesses tends to be more precarious due to the extensive managerial and technical deficits characteristic of minority entrepreneurs. In general, these deficits stem from a lack of formal business training. Other causative factors include the absence of an enduring entrepreneurial tradition, failure to find meaningful managerial employment, the typical undercapitalization of minority businesses, which leaves less room for error and little or no money for necessary assistance, as well as the unavailability of self-help aids for the minority businessman who seeks to develop his business skills. (4)

This study reiterated most of the statements made a decade ago. Minorities, although with some degree of college education still lack the necessary business training and an enduring entrepreneurial tradition. Previous experience in a managerial capacity was also minimal.
4. THE AGED

As individuals age, the level of financial position plays an increasingly important role in determining their degree of satisfaction with life. Many older individuals look upon Social Security as the road to happiness. However, more commonly, the combination of a fixed income and high inflation exacerbates the whole adjustment process to growing old. As one elderly individual recently remarked:

"You work your whole life putting by what you can, then you can't afford to retire. What a hell of a life!" (5)

Because the very real fear of running out of money before one dies is so strong, some individuals try to keep working past the age of 65. This is often not possible, however, because of mandatory retirement rules. On the other hand, individuals who own their own business do have an opportunity to keep working. Also, some retirees who have worked for wages all of their life find that the second income of a small business is needed in order to make ends meet.

Another aspect of a small business that makes it attractive to older persons is the fact that the business can serve as a social outlet. One respondent, who reported that he only made four or five dollars some days, said that his business was "just a place to hang out." Another interviewee, age 88, who had only six months earlier sold his lifetime business, said that he was going to start a blacksmith shop. His wife was encouraging him in this endeavor because she realized how bored he had been since his retirement.

There is nothing new about older persons continuing to work past the age of 65. Prior to the 1930's, nearly two-thirds of the U. S. population over the age of 65 was working. (6) However, with 25 percent of the population
unemployed in the early thirties, it was felt that a good way to create jobs would be to push the aged out of theirs. Consequently, the only reason so few old people work today is because their not working serves to solve a social problem. Similarly, there is no reason why small business owners would quit simply because a page is torn from the calendar.

The overall profile of the elderly business person is somewhat spotty. To begin with, there is apparently no listing of aged business owners. Thus, a sample could not be obtained. All organizations contacted by the authors, including the SBA, National Alliance of Senior Citizens, Gray Panthers, and SCORE, said that such a list of business owners would be very desirable but knew of no sources. Consequently, the following profile of aged small business owners is based upon a limited number of responses received to a general mailing list. Another factor that is often overlooked is that the aged small business owners do not constitute a homogeneous group in any sense of the word. The group is made up of varying age classes and varying races; some are part-time workers and some are full-time; some are rich and some are poor; some are healthy and some are infirm; some are willing to move to a warmer climate and some are not; and some are male and some are female. In short, there is not, on the surface, any factor other than artificial ones that distinguish the older small business owner from the young.

Because of the low number of responses received from aged small business owners, no attempt will be made here to analyze the results. The previous tables have included a column for the aged, but these results can only be considered preliminary since there is no statistical reliance that can be placed upon the figures.
5. SUMMARY AND CONCLUSION

This paper has compared the typical female, minority race, and aged small business owners to the typical business owner -- the white male. Several differences were noted. The female owner was more likely to be unmarried and younger than the male, although she started her business at the same age as he did. Thus, the woman has slightly less experience. Probably the most notable difference between males and females was that the woman gave her spouse a great deal of credit for her going into business.

The minority small business owner was six years younger than the white male and more often from a large city. Their goal of a better life for their family was the primary motivation for going into business.

As for future research, two areas became immediately obvious to these authors. First, since there is such a low percentage of minority owned businesses, it might be advisable to do a profile comparison between the minority small business owner and the minority non-owner. The second area where more research is needed is with respect to the elderly. A major effort needs to be put forth to determine who these individuals are.
REFERENCES


2. Michael Ferrari, Profiles of American College Presidents (East Lansing, Michigan: Division of Research, Graduate School of Business Administration, Michigan State University, 1970) p. 158.


1. EXECUTIVE SUMMARY

Minorities have not been able to participate fully in the ownership of businesses in SBA Region IV over the years. They own less than 9% of all regional businesses and obtain 0.6% of all regional business receipts. These firms are essentially retail and service businesses (74.5%) in no-growth areas, with limited capital, poor management, and marginal profits. The aim must be to increase the number and size of minority businesses in other industrial categories so that greater employment opportunity will be provided and increased profitability will result.

Recommendations

The supporting government policies should focus on three main areas: the entrepreneur, capital, and markets. The program for entrepreneurial development should:

1. Attract minority managers from majority-owned corporations, government, and the non-profit sector to own and control their own businesses. A package of incentives which would include pension considerations and guaranteed wages over some period could be provided.

2. Have a goal of making 20% of the graduates of business schools and colleges over the next ten years be members of the minority
population. This should be with the financial support of government, majority businesses, and foundations.

3. Include business internship program at majority-owned businesses for minority students from high schools and colleges.

The program for capital availability should include:

1. Increased government deposits at the minority-owned financial institutions (15% of all government resources).

2. Incentives for pension funds to invest in minority businesses.

3. Facilitating the establishment of Employee Stock Ownership Plans to take ownership and control of firms, such as occurred at South Bend Lathe, South Bend, Indiana. Minority management, however, should be instituted.

4. Expansion of the Loan Guarantee Program to include bonds for minority construction contractors.

The program for market development should include:

1. Increased purchases by government - 15% of all government purchases - and increased purchases by majority-owned corporations. A 20% per year increase in purchases by member corporations of the National Minority Purchasing Council for the next six years is desirable.

2. Emphasis on identification of viable businesses for sale, or a business opportunity for development, that could be exploited by minority businessmen. The minority business development centers would bring together the opportunity, the businessman and the capital.
3. Development of high-technology firms owned and controlled by minorities. This could be facilitated by the utilization of the products from space research.

The overall program should be continuously monitored, enforced, and evaluated so that tangible results can be achieved in the next six years.

2. THE GENERAL PROBLEM

Minorities in the American economy suffer in large part economic deprivation and social degradation. The black people which comprise 11% of the population are the sons of slavery and heirs of promise; consequently, they find themselves throughout many generations in a cesspool of poverty and illiteracy. The Spanish-speaking minority which are approximately 7% of the population are essentially migrants or their descendants from Puerto Rico, Cuba or Mexico. Because of their image as "wetbacks" or illegal immigrants and also their language barrier, they have not been socially accepted by the populace. The Chinese, Eskimos and Indians comprise less than 1% of the population. They have remained essentially isolated from the mainstream of American life. The Eskimos are in the extremely cold regions of the north, the Indians are on the reservations, and the Chinese are in the large city ghettoes, euphemistically called "China Towns."

The minorities have found it difficult to penetrate the social and economic life of the nation. In the area of economics, and particularly ownership of businesses, the record is dismal. Although they represent 18% of the population, they own less than 5% of all U.S. businesses, obtain only 0.7% of all U.S. business receipts, and provide employment for approximately 0.8% of the labor force. See Table 1.
Table 1

COMPARISON OF MAJORITY/MINORITY BUSINESS FIRMS

<table>
<thead>
<tr>
<th></th>
<th>Majority</th>
<th>%</th>
<th>Minority</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Firms (000)</td>
<td>8,730</td>
<td>95.6</td>
<td>382</td>
<td>4.4</td>
</tr>
<tr>
<td>Business Receipts ($000,000)</td>
<td>2,381</td>
<td>99.3</td>
<td>16.6</td>
<td>0.7</td>
</tr>
<tr>
<td>Number of Persons Employed (000)</td>
<td>56,466</td>
<td>99.2</td>
<td>456</td>
<td>0.8</td>
</tr>
</tbody>
</table>


The distribution of these businesses is as follows: construction, 10.0%; manufacturing, 2.6%; wholesale trade, 2.0%; retail trade, 33.5%; services, 33.0%; finance, insurance and real estate, 5.1%; transportation and public utilities, 8.3%. The predominance of minority businesses in the retail and service categories should be noted. Fully 66.5% of all minority firms are in these categories. See Table 2.

The receipts of these firms and their percentage distribution are also displayed in Table 2. The low percentage receipts from manufacturing 7.8%, transportation & public utilities 4.6%, and finance, insurance & real estate 5.2% should be observed.

It is necessary to juxtapose the number and receipts of minority-owned businesses to majority-owned businesses in order to get a better understanding of the dimensions of the problem. The relationship of the number and receipts of minority-owned firms to total business activity is presented in Tables 3 and 4.
Table 2
MINORITY-OWNED BUSINESSES BY INDUSTRIAL CATEGORIES

<table>
<thead>
<tr>
<th>Industry</th>
<th>Number of Firms</th>
<th>% Distribution</th>
<th>Total Receipts (000,000)</th>
<th>% Distribution</th>
<th>Average Receipts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail</td>
<td>121,399</td>
<td>33.5</td>
<td>7,477</td>
<td>45.8</td>
<td>61,600</td>
</tr>
<tr>
<td>Services</td>
<td>119,711</td>
<td>33.0</td>
<td>2,149</td>
<td>13.2</td>
<td>18,000</td>
</tr>
<tr>
<td>Construction</td>
<td>39,875</td>
<td>10.0</td>
<td>1,746</td>
<td>10.7</td>
<td>43,800</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>9,444</td>
<td>2.6</td>
<td>1,270</td>
<td>7.8</td>
<td>135,000</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>30,238</td>
<td>8.3</td>
<td>750</td>
<td>4.6</td>
<td>23,300</td>
</tr>
<tr>
<td>Wholesale</td>
<td>7,153</td>
<td>2.0</td>
<td>1,797</td>
<td>11.0</td>
<td>251,300</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>18,575</td>
<td>5.1</td>
<td>856</td>
<td>5.2</td>
<td>46,200</td>
</tr>
<tr>
<td>Other</td>
<td>15,965</td>
<td>4.4</td>
<td>292</td>
<td>1.8</td>
<td>18,290</td>
</tr>
</tbody>
</table>

Table 3
COMPARISON OF INDUSTRY DISTRIBUTION
OF NUMER OF FIRMS

<table>
<thead>
<tr>
<th>Industry</th>
<th>Minority Firms (000)</th>
<th>Percent</th>
<th>Majority Firms (000)</th>
<th>Percent</th>
<th>Total Number of Firms</th>
<th>Minority Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction</td>
<td>39,875</td>
<td>10.0</td>
<td>980,125</td>
<td>11.7</td>
<td>1,020,000</td>
<td>3.9</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>9,444</td>
<td>2.6</td>
<td>427,556</td>
<td>5.1</td>
<td>437,000</td>
<td>2.1</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>30,238</td>
<td>8.3</td>
<td>401,762</td>
<td>4.8</td>
<td>432,000</td>
<td>6.9</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>7,153</td>
<td>2.0</td>
<td>552,847</td>
<td>6.6</td>
<td>560,000</td>
<td>1.2</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>121,399</td>
<td>33.5</td>
<td>2,259,601</td>
<td>2.7</td>
<td>2,381,000</td>
<td>5.0</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>18,515</td>
<td>5.1</td>
<td>1,299,485</td>
<td>15.5</td>
<td>1,318,000</td>
<td>1.4</td>
</tr>
<tr>
<td>Selected Services</td>
<td>119,711</td>
<td>33.0</td>
<td>2,092,289</td>
<td>25.0</td>
<td>2,212,000</td>
<td>5.4</td>
</tr>
<tr>
<td>Other Industries</td>
<td>35,600</td>
<td>4.4</td>
<td>334,400</td>
<td>4.0</td>
<td>370,000</td>
<td>9.6</td>
</tr>
<tr>
<td>Total</td>
<td>381,935</td>
<td>100.0</td>
<td>8,348,065</td>
<td>100.0</td>
<td>8,730,000</td>
<td>4.4</td>
</tr>
</tbody>
</table>

## Table 4

**COMPARISON OF INDUSTRY DISTRIBUTION OF BUSINESS RECEIPTS**

<table>
<thead>
<tr>
<th>Industry</th>
<th>Minority Firms</th>
<th>Majority Firms</th>
<th>Total</th>
<th>Minority Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Gross Receipts</td>
<td>Gross Receipts</td>
<td>Total Receipts</td>
<td></td>
</tr>
<tr>
<td></td>
<td>(000)</td>
<td>(000)</td>
<td>(000,000,000)</td>
<td>Percentage</td>
</tr>
<tr>
<td>Construction</td>
<td>1,746,254</td>
<td>144,453,746</td>
<td>146.2</td>
<td>1.2</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1,270,718</td>
<td>814,029,282</td>
<td>875.3</td>
<td>.14</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>705,358</td>
<td>158,794,642</td>
<td>159.5</td>
<td>.44</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>1,797,244</td>
<td>347,602,756</td>
<td>349.4</td>
<td>.51</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>7,476,875</td>
<td>476,423,125</td>
<td>474.9</td>
<td>1.6</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>855,975</td>
<td>251,944,025</td>
<td>252.8</td>
<td>.33</td>
</tr>
<tr>
<td>Selected Services</td>
<td>2,149,081</td>
<td>93,350,919</td>
<td>95.5</td>
<td>2.3</td>
</tr>
<tr>
<td>Other Industries</td>
<td>544,897</td>
<td>27,045,113</td>
<td>27.6</td>
<td>2.0</td>
</tr>
<tr>
<td>Total</td>
<td>16,556,392</td>
<td>2,364,643,608</td>
<td>2,381.2</td>
<td>.7</td>
</tr>
</tbody>
</table>

In manufacturing, minority-owned firms are 2.6% of all minority firms, whereas majority-owned firms are 5.1% of all majority firms. The minority-owned firms are a dismal 2.1% of all manufacturing firms. The receipts of these firms are 7.7% of minority firm receipts, compared to 37.0% of receipts for majority-owned firms. Minority-owned firms receipts are 0.14% of all firm receipts.

In wholesale trade, minority-owned firms are 2.0% of all minority firms whereas majority-owned firms in the wholesale trade are 6.6% of all such firms. The minority-owned firms are 1.2% of all firms in the industry. The receipts of these minority firms are 0.51% of industry receipts.

In finance, insurance and real estate, a key industry for business development, minority-owned firms are 5.1% of all minority firms whereas majority-owned firms are 15.5% of such firms. The receipts of these firms are 5.2% of minority-owned firm receipts, compared to 10.7% for majority-owned firm receipts. Minority-owned firm receipts are 0.33% of all firm receipts in this industry. Minority firms are only 1.4% of the total number of firms in the industry.

Further examination of Tables 3 and 4 will illustrate business conditions for other industrial categories similar to those outlined above. The implications are clear. Minority businesses on the national level are a small proportion of the number of businesses, insignificant in terms of receipts and employment, and control less than 0.5% of the nation's business assets. (11) If minorities are to assume an important role in the business life of the nation, then clearly the number and receipts of minority businesses must increase.
Rationale for Minority Business Development Programs

The increase in the number and receipts of minority businesses will lead to beneficial effects on the society, the minority community, and the individual businessman.

The society will benefit because:

a) Jobs will be created from the increased business activity. The unemployment rate among minorities is very high. In some ghettos it is 40%. The unemployment rate among minorities will be lowered because approximately 90% of the employees of these firms are minorities.

b) Welfare benefits will decline due to the gainful occupation of these minorities.

c) Unemployment payments will decrease because minorities will now have jobs from which they can earn a living.

d) The crime rate will decrease particularly in the minority neighborhoods. When people have jobs they are inclined to engage in less criminal activity.

e) The tax revenues will increase. The increase will come primarily from individual income taxes, taxes on business income, and higher property taxes.

f) Minority businessmen will develop the expertise, experience, and knowledge from managing their own businesses that will enable them to assume policy-making roles in government and on the boards of major corporations.
The community will benefit because:

a) Competent minority businessmen will provide community leadership that will guide their constituency to be a significant force in the society.

b) Successful businessmen will provide role models for the youth so that generations of minority businessmen will be fostered.

c) The minority controlled foundations in the community will be provided with gifts and donations from minority businesses which will enable them to maintain their integrity and good judgment in the service of their communities.

d) The minority businesses will be able to exercise their civic responsibilities by financing projects that will lead to better minority communities.

The individual will benefit because the wealth and prestige he accumulates from being a successful businessman will enable him to realize his aims and ambitions in the society and his community.

3. STATE OF MINORITY BUSINESSES IN THE REGION

Our major concern is with Region IV of the Small Business Administration, which includes the following eight states: Mississippi, Alabama, Florida, Tennessee, Kentucky, North Carolina, South Carolina, and Georgia. It is fitting to look at the data from the last business census to get an idea of the state of minority businesses in this region.

Tables 5, 6, and 7 provide the regional data that are of interest on majority and minority-owned firms. There are approximately 72,050 minority firms in the region having total receipts of about $2.34 billion. This
### Table 5

**COMPARISON OF INDUSTRY DISTRIBUTION OF NUMBER OF FIRMS - SBA REGION IV**

<table>
<thead>
<tr>
<th>Industry</th>
<th>Minority Distribution</th>
<th>Majority Distribution</th>
<th>Total Number of Firms</th>
<th>Minority Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction</td>
<td>8,280 (11.4%)</td>
<td>56,320 (7.6%)</td>
<td>64,600 (12.8%)</td>
<td></td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1,790 (2.5%)</td>
<td>45,000 (6.2%)</td>
<td>46,790 (3.8%)</td>
<td></td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>4,220 (5.8%)</td>
<td>19,360 (2.6%)</td>
<td>23,580 (17.8%)</td>
<td></td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>740 (1.0%)</td>
<td>55,510 (7.4%)</td>
<td>56,250 (1.3%)</td>
<td></td>
</tr>
<tr>
<td>Retail Trade</td>
<td>36,920 (51.2%)</td>
<td>283,630 (38.2%)</td>
<td>320,550 (11.5%)</td>
<td></td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>1,530 (2.1%)</td>
<td>47,740 (6.4%)</td>
<td>49,270 (3.1%)</td>
<td></td>
</tr>
<tr>
<td>Selected Services</td>
<td>16,830 (23.3%)</td>
<td>217,690 (29.3%)</td>
<td>234,520 (7.1%)</td>
<td></td>
</tr>
<tr>
<td>Other Industries</td>
<td>1,740 (2.4%)</td>
<td>16,560 (2.2%)</td>
<td>18,300 (9.5%)</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>72,050 (100.0%)</td>
<td>741,810 (100.0%)</td>
<td>813,860 (8.8%)</td>
<td></td>
</tr>
</tbody>
</table>

Table 6
COMPARISON OF INDUSTRY DISTRIBUTION
OF BUSINESS RECEIPTS - SBA REGION IV

<table>
<thead>
<tr>
<th>Industry</th>
<th>Minority Firms</th>
<th>Majority Firms</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Gross Receipts</td>
<td>Gross Receipts</td>
<td>Total Receipts</td>
</tr>
<tr>
<td></td>
<td>(000)</td>
<td>(000)</td>
<td>(000)</td>
</tr>
<tr>
<td></td>
<td>Percent Distri-</td>
<td>Percent Distri-</td>
<td>Minority Percentage</td>
</tr>
<tr>
<td></td>
<td>bution</td>
<td>bution</td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td>306,820</td>
<td>25,266,000</td>
<td>25,532,820</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>275,310</td>
<td>111,169,890</td>
<td>111,445,200</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>104,610</td>
<td>10,567,000</td>
<td>10,671,610</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>280,500</td>
<td>93,442,300</td>
<td>93,722,800</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>876,300</td>
<td>70,035,600</td>
<td>70,911,900</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>182,200</td>
<td>12,076,000</td>
<td>12,258,200</td>
</tr>
<tr>
<td>Selected Services</td>
<td>270,750</td>
<td>13,866,650</td>
<td>14,137,400</td>
</tr>
<tr>
<td>Other Industries</td>
<td>40,100</td>
<td>273,000</td>
<td>313,646</td>
</tr>
<tr>
<td>Total</td>
<td>2,336,590</td>
<td>336,656,440</td>
<td>338,993,030</td>
</tr>
</tbody>
</table>

Table 7
COMPARISON OF AVERAGE RECEIPTS PER FIRM – 1972
REGION IV

<table>
<thead>
<tr>
<th>Industrial Category</th>
<th>Average Minority Total Receipts</th>
<th>Average Majority Total Receipts</th>
<th>Minority Receipts (as Percent of Majority)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail Trade</td>
<td>23,740</td>
<td>246,930</td>
<td>9.6</td>
</tr>
<tr>
<td>Selected Services</td>
<td>16,090</td>
<td>63,700</td>
<td>25.0</td>
</tr>
<tr>
<td>Construction</td>
<td>37,100</td>
<td>447,900</td>
<td>8.2</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>153,800</td>
<td>2,470,420</td>
<td>6.2</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>24,790</td>
<td>545,826</td>
<td>4.5</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>381,600</td>
<td>1,683,190</td>
<td>22.6</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>106,310</td>
<td>252,950</td>
<td>42.0</td>
</tr>
</tbody>
</table>

represents 0.6% of the total receipts reported by all firms in the region. The number of minority-owned businesses represents 8.8% of the total number of enterprises. The relationship of the number of minority-owned firms to total business activity is presented in Table 5, and a comparison of the receipts of minority- and majority-owned firms is presented in Table 6.

The low percentage of minority-owned firms and the receipts of these firms to total business activity is evident. In manufacturing, minority-owned firms are only 3.8% of the total number of firms and obtain a paltry 0.2% of the total receipts; in wholesale trade they are 1.3% of total firms and receive 0.3% of total revenues. Other industrial categories display the same low representation of minority firms to majority-owned firms. In finance, insurance, and real estate minority-owned firms are 3.1% of the number of firms and obtain 1.5% of the total receipts. In retail trade, although minority firms are 11.5% of the number of firms they obtain only 1.2% of the total revenues. The explanation lies in the small size (revenues) of the minority firms.

Table 7 displays the average minority firm total receipts and the average majority firm total receipts by industrial categories. For retail trade the average minority firm total receipt is $23,740, while the average majority firm total receipt is $246,930. Observe that average minority receipts are only 9.6% of average majority receipts.

It is thus established that minority businesses in Region IV are in a terrible state. Let us now examine some of the changes that have been occurring over the past few years due mainly to the efforts of the Federal Government.
4. MINORITY BUSINESSES IN REGION IV - YEARS OF CHANGE

The Georgia Institute of Technology did a study in 1977 of the Number and Characteristics of Minority Firms with Paid Employees in Georgia. (5) The study has applicability directly to the state of Georgia. However, since Georgia is typical of the states in Region IV, that is, two or three large cities where industrial and commercial activities are concentrated, with a large agricultural sector, it is fitting to look at the changes in minority firms in Georgia.

Table 8 illustrates the percentage change between 1972 and 1975 of the number and gross receipts of the minority-owned firm, by industrial categories. The number of construction firms increased 61% while gross and average receipts increased 118% and 36% respectively.

This analysis focuses on number and receipts of firms because it is believed that if minority-owned firms can grow in number and receipts, then this will imply other desirable goals such as increased profitability and greater employment opportunity.

The manufacturing sector shows a 23% increase in the number of firms and 136% increase in gross receipts. For wholesale trade the increases are 50% and 106% respectively, while selected services shows a 70% and 143% increase. These are desirable growth patterns for minority business enterprise. It should be observed that the percentage change in average gross receipts for transportation and public utilities, and also for retail trade is negative. This results from the large number of small operations that started over the period.

In another attempt to arrive at the changes in minority business since 1972, the Minority Business Highlight Reports from the Office of Minority Business Enterprise (OMBE) can be examined. The data applies only
Table 8
PERCENT OF CHANGE BETWEEN 1972 AND 1975: ALL FIRMS
(GEORGIA - ALL MINORITIES)

<table>
<thead>
<tr>
<th>Number of Firms</th>
<th>Gross Receipts</th>
<th>Paid Employees</th>
<th>Salaries</th>
<th>Average Gross Receipts</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction</td>
<td>61</td>
<td>118</td>
<td>35</td>
<td>95</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>23</td>
<td>136</td>
<td>51</td>
<td>78</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>60</td>
<td>54</td>
<td>50</td>
<td>31</td>
</tr>
<tr>
<td>Wholesale</td>
<td>50</td>
<td>106</td>
<td>100</td>
<td>72</td>
</tr>
<tr>
<td>Retail</td>
<td>80</td>
<td>46</td>
<td>45</td>
<td>133</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>44</td>
<td>75</td>
<td>35</td>
<td>104</td>
</tr>
<tr>
<td>Selected Services</td>
<td>70</td>
<td>143</td>
<td>80</td>
<td>103</td>
</tr>
</tbody>
</table>

Source: Industrial Development Division, Georgia Institute of Technology
Atlanta, Georgia, 1977.
to minority firms assisted by the Department of Commerce in the Region. These firms, however, form a significant portion of the viable minority firms in the Region, possibly between 40-50%.

In an analysis of OMBE assisted firms from January 1, 1974, to September 30, 1976, for the Region, a total of 2231 firms were identified as receiving technical assistance. (2) The largest number were in Florida, followed by Georgia and North Carolina. The firms assisted were highly concentrated in retail trade, 32%; selective services 23.8%, and construction 20.2%. The first two are normal. The construction industry has assumed a major role in the development of minority businesses. With the present requirement of 10% minority participation on all federal contracts the construction industry will assume greater importance for minorities.

In the survey, retail firms appear to be more concentrated in Mississippi, 42.3%; South Carolina, 36.8%; and Florida, 35%. Construction appears to be more concentrated in Georgia, 27.2%; North Carolina, 23.9%; and Tennessee, 22.1%. These percentages on industry concentration are in line with earlier figures. Construction was ranked first in gross receipts, replacing retail trade. Wholesale trade was again third in gross receipts. The average number of paid employees was 8.3, having increased from 6.6. The average gross receipts were higher for all industry sectors. This reflected the tendency for OMBE to help larger firms and also the emphasis on marketing assistance to raise the gross receipts of firms, particularly in construction and manufacturing.

In the Minority Business Highlight Report for Fiscal Year 1978, (3) the Atlanta region showed significant advances. The number of financial packages for businesses developed increased from 965 in 1977 to 1042 in 1978. The value of these loan requests rose from $41.31 million to $51.101
million. The number of procurements or marketing contracts rose from 1338 in 1977 to 1858 in 1978. The dollar value of these contracts to minority firms was up from $84.823 million to $92.143 million. The number of businesses receiving management and technical assistance increased slightly from 3175 to 3230 over the same period. This OMBE report reflects a good climate for the continued development of minority business enterprise.

In the Minority Business Highlight Report Mid-Year Fiscal Year 1979, (4) October 1, 1978, to March 31, 1979, the business indicators took a downturn. The number of financial packages processed declined from 473 to 353 while the dollar value of these loans fell from $26.072 million to $22.391 million over the six month period. The number of marketing contracts were down to 679 from 938 in the six-month period of a year earlier. The related value of these contracts fell from $43.384 million to $31.860 million. The number of businesses receiving assistance was down to 1467 from 2007 in the earlier period. Fortunately, this decline reflects government action rather than a general retreat from the minority enterprise effort. Federal funding for the Office of Minority Business Enterprise was reduced by $2.3 million and this resulted in a 12% decrease in the number of funded organizations and the consequent fall in the performance statistics. The Local Public Works Procurement Program was also phased out. This resulted in the significant decline in procurement contracts, for the construction industry.

The concern must be stabilize and improve the minority enterprise effort in the Region. This course of action is dependent on the economic outlook of the Region.
5. FUTURE DIRECTION OF MINORITY BUSINESSES IN THE REGION

The future direction of minority businesses in the Region is dependent on the larger economy. The economic outlook for the next decade remains strong. For the Southeastern economy, employment is up, construction is booming, and consumer spending remains ebullient. The dark clouds of inflation, unusually high interest rates, and excessive household debt should provide only a temporary setback to minority business progress.

The trend in population over the decade of the seventies for the eleven states in the Southeast has been positive. From 40.078 million in 1970 to approximately 48.102 million in 1978. The cold winters of the North coupled with the energy crisis has encouraged migration to the sun belt areas. The southeastern region has been the beneficiary of this migration. The outlook for continued population growth is strong. Thus a good labor force is assured and a firm demand for goods and services is evident. This discussion focuses on the eleven states of the southeastern United States which includes the eight states of Region IV. Because of the dominance of the eight states of Region IV in the southeastern economy, any discussion of the economic outlook of the Southeast applies to SBA Region IV.

The growth in total personal income in the 70's has been spectacular. From $137.873 billion in 1970 to approximately $292.108 billion in 1978. The per capita personal income has almost doubled over the decade from $3280 in 1970. The wages of production workers has climbed from $15.454 billion in 1970 to approximately $24.911 billion in 1978. The total cash farm income has grown from $10.874 billion in 1970 to $20.101 billion in 1978. The consumer purchasing power for minority businesses in the Region is strong, and this strength should continue into the decade of the eighties.
The expenditures for new plant and equipment rose from $4.501 billion in 1970 to approximately $10.710 billion in 1978. Construction contracts awarded increased from $15.806 billion to $36.920 billion in 1977. (7) The industrial demand for the goods and services of minority firms has been good in the seventies and should remain so in the eighties.

There has been no shortage of power during the decade of the seventies. Electric power production rose from 403.887 billion kilowatt hours to 577.369 billion kilowatt hours in 1977. Coal production was 189.386 million short-tons in 1970 and approximately 228.508 million in 1978. Petroleum production has been on the decline. From 1,012.207 million barrels in 1970 to 737.917 million barrels in 1976. This problem will soon be solved as factories switch from oil to coal and nuclear power for energy.

In looking at the financial institutions in the southeastern economy, there is firm growth in the seventies. Deposits at all commercial banks rose from $61.892 billion in 1970 to approximately $138.935 billion in 1978. Savings and loan deposits rose from $24.611 billion in 1970 to approximately $79.894 billion in 1978. Credit union shares increased from $2.198 billion in 1970 to approximately $8.125 billion in 1978. (7) The financial position of the Region is strong. The financial outlook for the decade of the eighties is solid.

As the eighties appear on the horizon the concern is to improve the role and importance of minority businesses in SBA Region IV. To accomplish this the appropriate strategies for change must be followed, and a full awareness of the problems as perceived by the minority businessman.

Perceptions of Minority Business Problems and Programs

In discussions and correspondence with minority businessmen in selected cities of the region such as Atlanta, Memphis, Tampa, St. Petersburg, Miami,
Jackson, and Birmingham, it was possible to get some of their views on minority business issues. A random selection of their comments follows:

... there is very little, or no real effort to help these small businesses. No loans, no credit, no proper support.

... existing laws on Equal Employment Opportunity and other fair business practices are not being enforced...a lack of commitment on the middle and lower levels of government.

... the minority bank deposit program, the 8(a) program, and all others should be in one agency.

... the cost of money is so high, and the administrative red tape including reporting requirements is so time consuming few minority owned businesses can grow.

... a better program to loan money to small business, and to get them business by way of contracts is needed.

... programs are poorly administered ... too vulnerable to rip-offs and half-hearted efforts.

... greater need in financing.

... business owners have to go through too much red tape to get operational capital.

... programs fine, but mismanagement of funds.

... difficulty in getting qualified employees.

... too many promises are never carried out.

... more corporations need minority purchasing programs.

... we need orders and contracts, not loans or advice on how to manage business we don't have.

... white-owned corporations will not do sufficient business with us, nor will city or U. S. government.
... often poor management of programs -- emphasis sometimes more on strict interpretations of legislation than helpful interpretations.

... there is a general reluctance by corporate America to do business with minority vendors. Same can be said about lending institutions in conjunction with SBA.

... bank will not give us a line of credit. SBA client caught between bank and SBA.

... unfulfilled promises. Many inquiries, little action, and much red tape.

... assistance programs should show how to market the business and offer assistance.

... programs are adequate, but they do cost the business a great deal of money in getting paperwork executed which government requires.

... the man with the ability to perform but not yet established, he can get no assistance.

... bonding for minority-owned companies is almost impossible. Insurance rates, working capital. Getting banks to finance jobs.

... company should be given counseling on how to grow and manage large contracts and shown how to offer competitive yet profitable bids.

... assistance programs need to give more guidance along with the money.

... lack of effective assistance, poor insurance, technical assistance, contracts, and enforcement.
... lack of positive controls to insure a ratio of the available contracts.

... bonding hard to get by Blacks.

... bonding impossible without SBA. Insurance rates much too high. Money very scarce.

With the full awareness of the problems of the minority businessman developed through analysis of the data and his own comments, attention can now be directed to recommendations.

6. RECOMMENDATIONS

It has been established earlier that minority businesses are an insignificant part of the businesses of Region IV in both number and receipts. It was noted that these variables are highly associated with the ability of firms to provide employment and income for an area. Consequently, we see that minority firms which are located largely in the economically depressed sections of the major cities of the Region are of little importance in generating jobs and income for the area. In the minority areas of such cities as Birmingham, Atlanta, Memphis, Greensboro, Charleston, Tampa, and Miami, unemployment averages 14% and teenage unemployment averages 35%. There is a circle of poverty here. Because these minority areas have limited income, the demand generated for goods and services of minority firms remain low, and consequently these firms remain small and insignificant in the economy. The concern must be to increase the number and receipts of minority businesses. This is our clear objective.

The focus must therefore be on programs to accomplish the objectives. These programs must be directed at:

1. The Entrepreneur

2. Capital

3. Markets

**Program - Entrepreneur**

The development of minority businessmen in the Region will take great effort from all levels of government, Federal, State, and local.

1. The minority business counsellors, financial analysts and market specialists who are at present working in the business development organizations of the region should all be encouraged and facilitated to enter their own businesses. Their experience, training and knowledge of businesses should enable them to avoid the pitfalls of other businessmen.

These business development organizations should be used as training centers for future minority businessmen. After a maximum of five years, every professional in these organizations should go into his or her own business or be fired.

2. Minority management professionals in majority-owned firms should be induced to seek ownership and management of their own firms. This can occur if the present business development organizations are staffed to develop financial packages for medium-sized businesses which are for sale. The businesses which must be divested by corporations due to anti-trust actions are a good starting point for these managers. It is clear that the necessary profit and income potential must be present to make it attractive for these managers to leave their secure jobs.

3. The Universities of the Region should have a goal of making 20% of their business school graduates over the next ten years be members of the minority population. This will ensure a pool from which potential minority
businessmen will come. Government, majority businesses, and foundations should finance such a program. Special programs patterned from the Basic Educational Opportunity Grants and the State Educational Opportunity Grants should be developed for minority business students.

4. The majority-owned businesses of the Region should engage in business internship programs for minorities. Appropriate rewards to these businesses should be developed (tax benefits). Each business should be induced to take ten interns annually for six years, either high school or college students. The high school graduates would be given scholarships to pursue a business degree after 12-24 months of business experience.

**Program - Capital**

1. The government at all levels should place 15% of their resources as deposits in the minority-owned financial institutions of the Region. This would immediately increase the lending capacity of these institutions so that they can make larger loans.

2. Banks which make loans to minority businesses should be more highly favored with government deposits. The government should deposit in these banks as a minimum, 50% of the value of the loans made.

3. All pension funds which invest in minority businesses should have a guaranteed minimum rate of return for their first seven years, equivalent to the highest rate paid on Treasury bills over the same period. The aim is to provide some incentive to the managers of pension funds to invest in minority businesses.

4. Employee Stock Ownership Plans should be established where feasible to take ownership of firms that are for sale, and minority management instituted. (See my article, 11).
5. A direct loan program should be developed which is aimed at making money available for minorities to purchase firms of sizes above $3 million in sales. This program could be coupled with a 90% loan guarantee program directed at the community development corporations that desire to acquire businesses. The minimum involvement of a community development corporation should be $100,000. This would enable these corporations to acquire larger-sized businesses.

6. A program of government guaranteed minority bonds for construction contractors similar to guaranteed loans should be developed.

Program - Markets

The strategies and programs for developing minority firms would be divided into those aimed at:

A. Market growth by internal expansion
B. Market growth through acquisitions

A. Market growth by internal expansion

1. The minority firms which have the capacity to supply goods and services to the government and large corporations should have 15% of all government contracts and a 20% per year increase in purchases by member corporations of the National Minority Purchasing Council for the next six years. Both the government and the Minority Purchasing Council should monitor these efforts. The aim is to enable the growth of these institutions and firms to benefit the minority community.

2. Market opportunities for new products and services should be identified by the minority business development organizations and these firms assisted to get contracts in these areas. The requirements would be high growth potential, high volume, low capital requirements, low technical skill of workers.
3. These firms should be assisted to recruit competent minority management personnel to direct their expansion and development. The establishment of a two-year wage guarantee program for key personnel should encourage them to accept employment in these firms.

4. The minority business development organizations should assist these firms to obtain equity and loan financing for their expansion.

B. Market growth through acquisitions

1. A program should be established which would aim at identifying viable businesses for sale that could be purchased by minorities. These would usually involve --

   ... family owned businesses;
   ... divestitures by corporations required by the anti-trust division of the justice department; and
   ... spin-offs of corporate divisions.

The minority business organizations should be professionally staffed to engage in this activity.

2. Development of minority firms in the high-technology fields should proceed apace. The fruits of space research and other high-technology programs funded by government should first be preferred to minorities for business development. (13) This would enable minorities to get in on the ground floor of the industrial giants of tomorrow. The National Space Technology Laboratory at Bay St. Louis, Mississippi, should be facilitated to search the NASA and Defense Department data banks for products which could readily be adapted to the consumer market. Examples of products already adapted but not by minorities are:

   ... sunglasses that really protect the eyes
compact video tape cameras
digital watches
fireproof clothing
smoke detectors for the home
and diagnostic and treatment equipment, such as CAT scanners (computer-enhanced X-rays).

7. CONCLUSION

Minority businesses have languished in the backwater of the American economy for too long. They have an important role to play in the integration of the society and the movement of minorities toward economic parity. This role cannot be fulfilled without massive government intervention in the effort. Only government can perform on the basis of a social conscience. The majority-owned firms will not act except profits can be realized. Years of deprivation and continued discrimination have left minorities without the asset base for meaningful business development through their own efforts. Significant government action is desired.

The state of minority businesses in Region IV has been examined, the desirability of business development explained. Recommendations have been broadly outlined. Let there be hope that some action will be taken.
References


1. INTRODUCTION

Initially, the intent of this paper was to explore the availability of data on research and development (R and D) activity of small firms in the Southeastern United States: data on characteristics of the entrepreneur, structure and characteristics of the firm, educational and experiential characteristics of employees, technical intensity of R and D, initial and current capital financing, and so forth. An ultimate objective would be to analyze such information for guidance in targeting resources regionally and according to those characteristics which might encourage technical activity and increase the likelihood of its success.

Various sources of information were approached until it became apparent that no significant data does, in fact, exist—at least not in a form suitable for analysis and as a guide to policy. The more essential question then suggested itself: If an appropriate policy objective is to encourage research and development among small business firms, and if there is no useful source of information to guide the allocation of resources toward this end, then what mechanisms can be put into place for collecting needed information? The answer seemed to lie with the technical institutions which are the source of much research and development activity.

Thus, this paper focuses on firms which may be classified as spinoffs from a technological institution, the Georgia Institute of Technology. Section 2 defines "university spinoffs." Section 3 attacks the problem of measuring spinoff activity. Early spinoffs from Georgia Tech and the attitude
of the University toward them are the topics of sections 4 and 5. Section 6 reports the results of interviews with a sample of recent spinoffs along with some tentative conclusions regarding the relationships between entrepreneurs and the University.

In general, this preliminary study produced more questions than answers, with the following being more evident:

(1) What are the circumstances in an institution which promote or hinder the spinoff phenomenon? And specifically, what conditions in small business firms are or can be duplicated in universities to give support and encouragement to entrepreneurship? On the other hand, what institutional characteristics are barriers to spinoff activity, to be avoided if the university is to become the central part of a critical mass of innovation for its region? How can the university attract and exploit key researchers who will act as a wedge into emerging areas of science and technology? How can research personnel be exposed to circumstances conducive to technical entrepreneurship?

(2) For the functioning small business firm, what support facilities should the university develop to enhance the survival potential of its offspring? How can the university help to establish the firm's credibility in the marketplace and within the financial community?

(3) For local governments, what program procedures can be most cost-effective for encouraging technical development? How can communities identify potential gaps in planned scientific complexes and what steps can be taken to fill them?

(4) For venture capital firms, small business investment companies, and private investors, what characteristics of technical firms indicate less risk? To what extent should private lenders take a "developmental" interest in potential borrowers as opposed to a merely "judgemental" assessment of
the firm's prospects?

2. UNIVERSITY SPINOFFS

The most sophisticated research and applications of new technology are frequently conducted by firms classified as university spinoffs. A spinoff is defined as a commercial enterprise founded by an employee (academic faculty member, researcher, technician, or administrator) as a direct result of ideas or skills developed through employment at the university.

In general, spinoffs embody advanced scientific or engineering skills which require specialized education, but spinoffs may also be defined to include non-technical enterprises in which particular industrial or management skills may be required for successful growth. Even this definition may be too restrictive as a measure of technological development directly promoted by universities. A complete list of spinoffs should probably include enterprises begun by graduate students and those supported in a meaningful way by the resources of the university. Moreover, in many cases "secondary spinoffs"—spinoffs from other spinoffs—may be found to extend further the technical impact of the university on the community and the region.

Researchers from the academic, financial, and research communities have addressed the spinoff phenomenon as it applies to some of the nation's largest universities, research organizations, and industrial companies, but none has yet examined the spinoff population from a major Southern university in a detailed and systematic way. The South's rapid growth in recent years suggests that there is fertile ground for investigation, from which valuable insights may be gained into the further question of the impact of technology on regional development. This paper will lay the groundwork for establishing a continuing source bank of information concerning spinoff
activity directly attributable to the Georgia Institute of Technology. The proposed collection would serve as a source of data regarding the characteristics of entrepreneurs and firms, the relative success of new technical enterprises, and their technical impact on the region.

3. MEASURING SPINOFF ACTIVITY

Unfortunately, identifying university spinoffs is difficult in the absence of a systematic procedure for reporting. Unlike private companies, universities cannot take equity positions in new firms; they have no well-defined mechanism for recording the progress or even the existence of spinoff firms.

The incompleteness of the data has probably contributed to a belief that universities function significantly less well as incubators of new technology than do industrial concerns. Some researchers have found a lower than expected spinoff rate from many universities, including such highly regarded institutions as Stanford (Cooper, 1971). Among universities studied, Massachusetts Institute of Technology appears to have the best record, having spawned an exceptional number of spinoffs constituting the "Route 128" complex of technical firms. Other successful producers of spinoffs are the University of Michigan/Ann Arbor, the University of Minnesota, and the University of Texas. Even university affiliated research parks and programs of commercial product development appear to perform rather weakly as bases for spinoffs. This is true also of independent research parks, in spite of their acknowledged contribution to regional industrial development.

Arnold C. Cooper (1972) has calculated spinoff ratios for universities and non-profit research groups according to number of spinoffs relative to average employment. The spinoff rate for government laboratories was
lowest at .0005, with a probable explanation being an orientation which is more theoretical than commercial. Research groups had a ratio of .0015; in contrast, universities had a ratio of .0082 when only engineering faculty was included in the base and only .0014 when engineering, physical science, and business faculties were included. Relatively greater success was reported by industrial firms, in particular smaller firms. Using a rather small sample, Cooper recorded spinoff rates of from .0710 for the smallest firm to .0003 for the largest, with an average of about .0015 for the large firms. A similar pattern of spinoff rates was found in a study of four M.I.T. laboratories; spinoff rates were found to be inversely related to laboratory size measured in terms of total funding.

Cooper's findings suggest some common characteristics of successful incubator institutions. They are small in scale (fewer than 500 employees) and they employ primarily research-oriented people. The inverse relationship between size and spinoff rate has several explanations. Small organizations are more likely to be working on projects of a scale appropriate to spinoff development. Their personnel are forced to develop a variety of capabilities in keeping with a broad range of responsibilities; close contacts within the organization make it possible to assemble an entrepreneurial team. Small organizations are more likely to comprise individuals of an independent bent, a higher percentage of whom are professional technicians. In some cases, small units may be less well managed than large units, providing a source of frustration to talented employees.

Investigation of the spinoff phenomenon will contribute toward an understanding of the university's impact on its region. But the results may be misleading in that they necessarily understate the real value of the university in promoting technical development. Edward B. Roberts (1972)
has referred to the "iceberg" problem which conceals much of the university's actual impact. The lack of spinoff data itself has already been mentioned, but other aspects of the university/industry relationship are often overlooked as well. For example, the university functions as an agent for technology transfer even when university entrepreneurs are not principals in the enterprise. University personnel may be instrumental in setting up a new manufacturing division of an existing firm, adding diversification and market flexibility to a stagnant enterprise. Or they may be responsible for establishing an entirely new operation: acquiring land, designing buildings and equipment, training personnel, researching the market, and even acquiring a small business loan for a new enterprise. And universities supply technically trained people to established firms and opportunities for continuing education to employed professionals.

With these caveats in mind, we have investigated this aspect of the Institute's impact on regional technical development. We began with a study of early spinoffs (1946-1969) and then solicited the names of firms established in the most recent decade. Identifying spinoffs was a difficult process without a systematic procedure for keeping records. We contacted department heads, school administrators, laboratory directors, and other technicians for their personal knowledge. Our resulting list of seven new firms and two well established firms is not comprehensive; but the enterprises seemed to be representative of a range of activities and capabilities worthy of investigation.

Interviews were scheduled with the principals in most of the firms. The respondents were helpful and enthusiastic about the project, in general, contributing from one to two hours to discuss the problems and needs of small technical firms.
4. EARLY SPINOFFS FROM GEORGIA TECH

Georgia Institute of Technology began a Doctor of Philosophy program in 1946 and awarded its first degree in 1950. The Georgia Tech Research Institute was incorporated in 1945, making the services of the Georgia Tech Engineering Experiment Station available to private industry on a contract basis. These actions established a basis for expanded university research programs and for valuable interaction between the university and industry. We might identify this period as the origin of the spinoff phenomenon for Georgia Tech.

The process began vigorously. A study completed in 1969 by Frederick C. Apple identified 29 Georgia Tech spinoffs with total annual sales of more than $23 million. More than half the early spinoffs examined were engaged primarily in consulting, and only one-fourth were primarily manufacturers. The remaining firms performed research and manufacture, marketing, or finance. The founders of the 29 spinoffs were predominantly university researchers, with only eleven firms founded by professors from academic departments. The firms employed 1,375 people: 820 nonprofessional personnel and 555 professional, of whom 66 were Georgia Tech graduates.

The consulting firms in the 1969 study were engaged primarily in the fields of architecture; computer systems and software; electronics and electrical engineering; mechanical, electrical, or civil engineering; water pollution control; housing development; and economics, engineering, and management on a systems basis. Manufacture included instruments, electronic components, fused ceramic oxides, chemical isotopes, and small prototypes.

University spinoffs have a particular advantage: A university researcher typically is working toward solution of a problem posed by a private firm. Understanding the technical aspects of a problem while communicating with a potential user of the solution provides a new entrepreneur
with "market knowledge." The spinoff firm may even have a guaranteed customer at the time it is first established. Beyond that initial market, however, the Georgia Tech spinoffs reported problems of reaching additional buyers. Many diversified to improve their growth rate, and a few failed to survive. (Of the 27 firms operating in 1969, at least 19 were still functioning ten years later.)

Early spinoff firms reported other advantages involving the continuing use of Georgia Tech as a source of valuable support toward the firms' development: library services, technical expertise for help with specific problems, additional personnel including part-time graduate students, and computer services. A few of the firms mentioned Georgia Tech as a market for their product and as a source of licenses and patents.

5. ATTITUDE OF THE UNIVERSITY TO SPINOFFS

The value of spinoff activity to the university depends on the relationship between benefits and costs. Possible benefits include intellectual stimulation for graduate students, greater interaction between university and industry, and development of an entrepreneurial climate for faculty and students. Some costs might be: neglect of academic duties in favor of proprietary interests, decline in emphasis on undergraduate instruction, and over-emphasis on applied as opposed to basic research. Many universities regard spinoffs as a potential source of faculty at some point in the future. They believe the experience gained in establishing a small business is a healthy attribute for teaching faculty. The professor's increased awareness of industry's needs adds relevance to classroom activities (Mahar and Coddington, 1965).

A favorable attitude toward spinoff activity may be camouflaged by the rather casual nature of a university's support for new enterprises. Frequently, the reason lies in certain political or legal restraints: a
consensus in the community that public resources should not be converted toward private purposes for private gain; prohibitions in some states against certain cooperative activity between university and industry; and occasionally an anti-industrial bias among the personnel of some institutions, although this is not generally a factor in engineering institutions.

When more direct channels for support are closed, support for development of advanced technology may take another form—in particular, the licensing of new technology to private investors. Even this activity poses legal problems when the user of university research is a large firm and subject to antitrust restrictions on exclusive licensing.

6. RECENT SPINOFFS AND CONCLUSIONS

The eight firms consulted for information in preparing this report represented a wide range of characteristics. There were manufacturing firms in electronics, chemical testing equipment, and instructional equipment for direct energy conversion; there were firms in general research and ecological research and in the use of computer cartography for land use planning. One principal and one co-founder were women.

The oldest firm in the group was 16 years old; the youngest less than one. Number of employees ranged from none to 200, and profits from negative to substantial (18% of sales). Annual sales ranged as high as 10 million. In general, the level of technology was high, with most firms describing themselves as operating "on the cutting edge of technology." Clearly, there is basis for the expectation that Georgia Institute of Technology could serve as a hub of technological development for the Southeast.

Within this range, there were significant similarities in the experiences of these firms. The entrepreneur was more likely to be in his or her thirties and was slightly more likely to have been associated with the university in a research than academic capacity. With minor exceptions (e.g., temporary
head of academic department), the entrepreneurs' only business experience was in contract administration. All the entrepreneurs reported strong character motivation: the desire to achieve, to be one's own boss, to respond to challenge, and the drive to produce a unique and useful product. Only one named a role model.

In the oldest firms, the entrepreneur reported some dissatisfaction with his or her employment experience at the Institute. It was felt that institutional limits inhibited aggressive leadership and preserved a provincial attitude toward new developments. As a result, the Institute failed to realize its potential for promoting regional progress. Most felt a degree of rejection or lack of appreciation by the Institute of what was felt to be his or her special capabilities. Whereas none reported active attempts to discourage entrepreneurial activity, none reported having received support or recognition. Newer firms expressed the tentative view that current attitudes may be different, and one stressed the financial and technical fruits which might flow to the Institute if entrepreneurship were to be more actively encouraged.

Ironically, the perceived negative attitude of the Institute toward entrepreneurship may have been the spur which brought out latent tendencies in that direction. If this is correct, the appropriate policy for encouraging technical entrepreneurship would seem to be to forbid it! Nevertheless, the older firms in this sample seemed to feel that the potential for success would have been enhanced if the Institute had provided services supportive of their needs.

There were similar organizational and growth patterns among the firms. One firm reported access to venture capital, but outside financing was minimal in all the firms. Several firms reported using public financing such as industrial development bond programs and urban development loans. Aside from financing, the most commonly expressed need was help with marketing.
Early customers were generally the result of contacts made at the Institute. Marketing procedures included: advertising in industry trade journals, exhibits in trade shows, sales representatives, regular newsletters, personal contracts and referrals, brochures, and a slide show. Many of the firms reported employing marketing consultants, generally with favorable results; but many marketing devices were found to generate few benefits relative to their high costs for the small firm. Two of the firms reported international sales, and one operated a Domestic International Sales Corporation. The State Department of Industry and Trade and Atlanta Chamber of Commerce were helpful in making international contacts and providing information on procedures.

Most of the firms reported some continuing relationship with a customer first encountered at Georgia Tech. Government contracts for manufacturing did not last long, however. The cost-plus-fixed-fee bidding procedure was a problem for small firms. Without full information on development costs, a firm might underbid unknowingly, or a firm might do so intentionally so as to gain business. In either case, competition was imperfect and often resulted in serious losses for the small R & D firm.

The more technically sophisticated firms in the group found difficulty hiring sales personnel with the technical background for marketing their equipment. In general, there seemed to be a problem of finding highly skilled technical workers or jobbing out technical work, in spite of the proximity to various technical institutions.

Most of the firms engaged in some sort of sales engineering, tailoring their product on the basis of feedback from buyers. Most were able to achieve a degree of standardization, with fixed pricing and improved profitability. In general, there was little competition, evidence of the advanced technology of these firms. However, some acknowledged that expanding markets were bringing on the threat of competition. As suppliers of research and equipment
to such growing activities as solar technology, measurement of radiation, energy management, electronic and chemical testing, land use planning, and ecological research, these firms are responding to unfilled demand and enjoy healthy potential for growth.

The firms reported no significant use of Georgia Tech resources. The library, consulting services, investigations of technical instrumentation, and some employment of students were cited as of limited value. One firm reported some dissatisfaction with the quality of consulting available at the Institute. It was felt that Institute personnel are not sufficiently alert to the most recent developments in their fields of specialization. The problem may be characteristic of the Southeast where farmers and business people see little relationship between their concerns and the activities of the university. The perception that the university is aloof from regional problems appears to be reflected in little voter support for university funding. In turn, the lack of funds limits the ability of the university system to attract high level specialists in areas important to regional technical development.

Apart from technical expertise, the university could also be a vehicle for valuable management consulting on such topics as: merger law and typical results of mergers; alternative financial programs; production cost analysis and pricing.

There are other needs which could be served easily by the Institute: the use of specialized equipment and facilities such as film processing; the use of excess space; greater use of high quality scientific and engineering talents of the Institute. An even more valuable service would be for the Institute to seek out contract opportunities for subcontracting to small businesses. Another would be to make available the Institute library.
catalogue on microfiche to research firms and to provide book delivery at nominal cost.

The university could be the instrument for producing seminars proving inter-communication among technical entrepreneurs. The university has the infrastructure and contacts for coordinating such seminars and could gain visibility in the technical community. Seminars of this type should include (as guests rather than participants) top level administrators of programs geared to using and aiding small firms. Some seminar topics might be: principles of sales management, management of research and development, small business accounting, technical writing, and inventory control. This proposal suggests that the university coordinate and house such activity but that actual planning and the actual conduct of the program be the responsibility of small business firms themselves.

In general, entrepreneurs felt the Institute could serve more effectively as a hub of technical resources in the area if it would amend its attitude toward spinoffs. The view was that the Institute should adopt a more "umbrella" attitude as opposed to what is perceived to be a more exclusive "proprietary" attitude toward spinoff activity. An improved interaction between the academic and industrial environments, it was said, would enhance the technical capacity of both. One respondent expressed this view: Lacking funds to attract Nobel Prize winners, a state institution could instead gain funds and visibility through support of and encouragement to applied technology.

The Small Business Administration received both praise and blame for its efforts in behalf of technical entrepreneurship. The SCORE program and ACE were generally rated as helpful or extremely helpful. Only one respondent reported a poor match between his company's needs and the retired executive enlisted by advice through SCORE. Weekly seminars conducted at Emory University were also praised, although the usefulness of particular sessions
depended strongly on the person conducting the program. An even more effective SBA program might be to establish a Small Business Association of persons who meet monthly for dinner and a speaker on a topic of small business concern. The chief result of such a continuing relationship would be to establish communication among small business people themselves. Among principals of small business there is the enthusiasm and energy for creative growth, the perception of common problems and the willingness to share responses to these problems. Many small business people feel that it is a mistake to enlist university personnel and persons from large corporations in the solution of problems they have not themselves experienced.

SBA's Technical Assistance Program was mentioned as a valuable source of information, but the feeling was that the service was not sufficiently publicized to gain widest benefits. In this case, the SBA could set up small companies to provide particular services in such areas as marketing management, inventory control, literature searches, and accounting services for research firms. Of particular value would be a service instructing firms on procedures for doing business with government; part-time help in completing government forms would also be welcomed.

None of the firms I visited had acquired SBA loans and most cited the red tape and the minority focus as reasons for not applying. One firm praised SBA's bid and performance bonding programs as particularly valuable for small firms. They recommended that funds be more forthcoming for such major expenditures as equipment investments and that a portion of Federal contract money be earmarked for small R and D firms (this last in recognition of the fact that proposal writing is a more costly activity for small firms than it is for the large firms). Some firms pointed out that government receivables are slow in paying and do not include interest or indirect research and development costs.
They would like to see the SBA attempt to match up government contracting with small business capabilities, particularly in research and development. The procedure might be to enlist a university as prime contractor and overseer of a project, lending credibility and at the same time establishing strong industry ties with the university.

Additionally, the SBA could help to bring private investors together with new firms, providing some guarantees or tax incentives for highly technical ventures. Adequate funding would enhance the firm's ability to compete with established firms in areas of fine specialization.

If there is a common thread running through the comments of these entrepreneurs, it is the drive toward application - toward responding to a perceived need by adaptation of new technology. Most of all they want vehicles for communication: among themselves, with experts in the sciences and in management, with potential users of their services. A greater sense of complementarity and of flexibility in established institutions would enhance their individual prospects as well as the technical prospects of the region.
REFERENCES


THE ROLE AND DEVELOPMENT OF THE CARPET INDUSTRY: A MARKETING PERSPECTIVE

Dan H. Robertson
Georgia State University

1. THE CARPET INDUSTRY IN FEDERAL REGION IV

This paper analyzes the marketing practices of the carpet industry in Federal Region IV. This first section presents a very brief historical background, as well as the current situation of the industry and concludes with an inventory of currently available data on the carpet industry in Federal Region IV.

The second section deals with the marketing practices of the industry in this region. Of particular note in this section is the application of a marketing audit technique which will be explained later. The paper concludes with the third section which will provide recommendations for change in current marketing practices based upon the information gleaned from sections one and two.

Historical Background

While the specific origins of the carpet industry are lost in history it appears to have originated in the Middle East in ancient times (Bigelow-Hartford Carpet Co., 1925). As trade was established between the Middle East and Europe, the industry spread to Europe, notably to England (Bartlett, 1978). With the industrial revolution in England, the productive capacity for carpet increased dramatically. From England, carpeting spread to the American Colonies. During the Revolutionary War, many domestic households produced their own carpet. This resulted in a rich mixture of hand-hooked or braided...
rugs, but these were again intended primarily for consumption within the household where they were produced. William Sprague is generally credited with opening the first carpet mill in the United States in 1791 (Cole and Williamson, 1941).

Most histories of carpet production focus upon the period 1825-1839 as the start of the U. S. carpet industry. The growth of the industry was significantly aided by the invention of the power loom in 1839 by Erastus D. Bigelow. The early U. S. carpet industry was centered upon the Northeast, which was also of course the center of population at that time.

In the latter 1800s, with the growth of the cotton industry in the South and Southeast, the carpet industry spread to the region which is the focus of this paper (Federal Region IV). It was not until after the Civil War that this industry made the transition, however, from home production to factory production in the Southeast.

Current Situation

It is important to note that when we speak of the carpet industry in Federal Region IV we are speaking almost exclusively of the manufacturer of tufted carpeting. The production of tufted carpeting is a fairly recent phenomenon having starting in a post-World War II era. Thus, the industry is in reality a very young industry, roughly thirty years in age. Conversion from a woven process to a tufted process was complemented by the availability of backing compounds after World War II.

Today approximately one-half of the entire industry output of tufted carpet originates in the Dalton, Georgia area (Hightower, 1979). It is also important to note that the Dalton area has approximately 150 carpet-producing mills and is also the home of the Carpet and Rug Institute (CRI).
Inventory of Available Data

Four basic sources of data were located in the research for this paper. The most complete body of data available on the carpet industry in Federal Region IV was obtained from the Carpet and Rug Institute. A particular debt of gratitude should be acknowledged to Mr. Wendell H. Thomas, Marketing Director of CRI, who made personal time available for interviews and provided much of the background research reflected in this paper. The Carpet and Rug Institute is a trade association of approximately 300 carpet distributors and manufacturers.

A second body of data consists of the published literature dealing with the carpet industry. U. S. government documents, doctoral dissertations, published books on the industry, and articles in trade publications form the basis for this body of literature. A complete listing of the sources used in the writing of this paper will be found in the references listed at the end of this paper.

A third source of information is provided by the few empirical studies which have been done on this industry. These sources are very limited in number and somewhat outdated.

A fourth and last source of data consisted of personal interviews with individuals connected with the carpet industry. Individuals interviewed came from both the trade association (CRI personnel) and manufacturers of carpeting (mill personnel), as well as (marketing personnel) from carpet distributors and retail outlets (sales personnel).

2. MARKETING PRACTICES OF THE INDUSTRY

It is now appropriate to turn our attention to the marketing practices of the carpet industry in Federal Region IV.
Current Market Environment

Prior to an analysis of the current marketing practices of the carpet industry, it is necessary to understand some of the basic facets of the industry's current environment. Key factors include:

- Carpet is a product which is in the early maturity stages of its industry growth cycle.

- Forecasts for the carpet and rug industry for the next few years indicate a slow but continual growth in total shipments (Carpet and Rug Institute, 1978).

- This is an industry characterized by many producers (carpet mills) most of whom have established little product differentiation in the marketplace.

- This industry is characterized by a great deal of price competition at the retail level.

- The industry has engaged in relatively little consumer education resulting in a great deal of consumer confusion regarding qualities, types of fibers used in production, (Man-Made Fiber Producers Association, Inc., 1978), installation, and maintenance of carpeting.

- Marketing strategies in this industry are either underdeveloped or nonexistent.

- Comparatively little use of marketing segmentation has taken place within this industry.

These key factors must be put in the context of the current economic situation. Like any other industry, current situation of the carpet industry is affected by the current economic uncertainty. The industry anticipates the continuation of inflation, no serious shortages of raw materials and a high probability for a business slowdown in 1979 (Carpet and Rug Institute, 1978).

Any product may be conceptualized as passing through four chronological stages in its life cycle. As depicted in Figure 1, when products are first invented, they are introduced to the marketplace resulting in initial sales volume and this sales volume continues to increase through the second stage (growth) and into the first part of the third or maturity stage and then sales
for the product begin to decline. Most industry observers believe that carpet is in the early maturity phase of its product life cycle. If continual growth is to be realized in this industry, then "spin offs" or additional new products, such as the use of carpeting for wall hangings, artificial grass carpeting, etc. must be developed.

FIGURE 1
Product Life Cycle Concept

Total industry shipments of carpets and rugs amounted to 1,024,572,000 square yards in 1977. As may be seen in Figure 2, this represents an increase of slightly over 9% when compared to 1976. It may also be seen from Figure 2 that although the industry experienced a downturn in 1975, shipments have increased in each of the two following years. At the time of this writing, 1978 figures were not available. However, a forecast prepared for the 1978-1983 is available (see Figure 3) and reflects a slight increase in each successive year.

Although few empirical studies have been done in this industry, the
studies which have been done provide support for the argument that the industry has established relatively little product differentiation. That is to say, few consumers recognize differences in the quality of various brands of carpet. In the pioneer marketing study done of consumer attitudes

FIGURE 2

Total Industry Shipments of Carpets and Rugs, 1973-1977

Source: The Carpet and Rug Institute Industry Review, 1977-78,
FIGURE 3

FORECAST FOR THE CARPET AND RUG INDUSTRY, 1978 - 1983

SQUARE YARDS - MILLIONS

(Percentages denote change from previous year)

<table>
<thead>
<tr>
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<th></th>
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<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>S.Y.</td>
<td>S.Y.</td>
<td>S.Y.</td>
<td>S.Y.</td>
<td>S.Y.</td>
<td>S.Y.</td>
<td>S.Y.</td>
</tr>
<tr>
<td>TOTAL INDUSTRY</td>
<td>+ 9.1</td>
<td>+ 7.5</td>
<td>+ 5.4</td>
<td>+ 5.6</td>
<td>+ 0.4</td>
<td>+ 6.9</td>
<td></td>
</tr>
<tr>
<td>Total Woven</td>
<td>- 13.2</td>
<td>- 1.4</td>
<td>- 3.2</td>
<td>- 1.3</td>
<td>- 2.0</td>
<td>- 3.4</td>
<td></td>
</tr>
<tr>
<td>Total Tufted</td>
<td>+ 9.8</td>
<td>+ 7.7</td>
<td>+ 5.6</td>
<td>+ 5.8</td>
<td>+ 0.4</td>
<td>+ 7.1</td>
<td></td>
</tr>
<tr>
<td>Total All Other</td>
<td>+ 2.5</td>
<td>+ 4.3</td>
<td>- 0.6</td>
<td>+ 2.5</td>
<td>+ 0.7</td>
<td>+ 1.7</td>
<td></td>
</tr>
</tbody>
</table>

for the American Carpet Institute in 1948, personal interviews were conducted with 6,122 respondents. One of the key purposes of this study was to determine the factors which influence the choice of a carpet. The overwhelming majority (76%) of the respondents gave the color or pattern of carpet as the single, most important reason for their selection of a particular type of carpet.

In 1961 the American Carpet Institute sponsored a more comprehensive study which obtained responses from 1,545 families which had purchased carpet in the six months prior to interview. National Family Opinion Incorporated, the marketing research firm conducting this study, found that over 40% of the respondents did not know what brand they had purchased and that there was a much greater recognition of carpet by store name (name of retail store where the carpet was purchased) than by the carpet manufacturer's brand name. When the 1961 study sought to establish major factors affecting the choice of a carpet, it found that color or pattern was again the single, most often mentioned factor. Figure 4 presents the full array of reasons given for a choice of purchasing a particular carpet.

Although these studies are dated, the information currently available would tend to support these studies in concluding that within the carpet industry little product differentiation has been established (Reynolds, 1968).

When a convenience sample of current carpet advertising was examined, price appears to be the single, most often mentioned factor. As noted in Section one, 50% of the total tufted carpet production is located in the Dalton, Georgia area. Since this area is transversed by a major interstate highway (I-75), even a casual tourist passing through cannot help but notice the multitude of billboards and outdoor advertising efforts which emphasize the ready availability of carpeting at a "bargain" price. Frequency and use of pricing is not to be unexpected given the earlier established lack of
FIGURE 4
Factors Affecting Choice of Carpet

<table>
<thead>
<tr>
<th>Factor</th>
<th>% of Respondents Mentioning</th>
</tr>
</thead>
<tbody>
<tr>
<td>Color or Pattern</td>
<td>37.0%</td>
</tr>
<tr>
<td>Price</td>
<td>17.7</td>
</tr>
<tr>
<td>Quality</td>
<td>11.8</td>
</tr>
<tr>
<td>Durability</td>
<td>9.9</td>
</tr>
<tr>
<td>Fiber</td>
<td>6.7</td>
</tr>
<tr>
<td>Other</td>
<td>16.9</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>100.0%</strong></td>
</tr>
</tbody>
</table>


product differentiation within the industry. This emphasis upon price of course has a negative impact upon total industry profitability. Figure 5 presents a wholesale price index comparing soft surface floor coverings, new passenger cars, and all commodities for the years 1950-1977.

An examination of the statistics in Figure 5 will reveal that carpeting clearly represents a consumer bargain when compared to the price of either automobiles or all commodities. However, while the consumer may be getting a bargain, the industry may be suffering from the intense retail price competition on carpet found in many areas.

On an overall industry level, the carpet industry has done very little to educate the consumer as to the quality and features of their product. Although a few of the larger manufacturers of carpet and fibers provide educational material for consumer use, such a practice is unusual in this industry. Figure 6 presents some illustrations of the types of educational
materials designed for consumer use made available by a very limited number of carpet or fiber producers.

FIGURE 5
Wholesale Price Comparison: Soft Surface Floor Coverings, New Cars and All Commodities, 1950-1977

<table>
<thead>
<tr>
<th>YEAR</th>
<th>SOFT SURFACE FLOOR COVERINGS</th>
<th>NEW PASSENGER CARS</th>
<th>ALL COMMODITIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td>104.7</td>
<td>78.5</td>
<td>81.8</td>
</tr>
<tr>
<td>51</td>
<td>131.2</td>
<td>81.9</td>
<td>91.1</td>
</tr>
<tr>
<td>52</td>
<td>109.9</td>
<td>87.9</td>
<td>88.6</td>
</tr>
<tr>
<td>53</td>
<td>111.1</td>
<td>87.6</td>
<td>87.4</td>
</tr>
<tr>
<td>54</td>
<td>107.7</td>
<td>88.2</td>
<td>87.6</td>
</tr>
<tr>
<td>55</td>
<td>110.6</td>
<td>90.9</td>
<td>87.8</td>
</tr>
<tr>
<td>56</td>
<td>113.6</td>
<td>95.5</td>
<td>90.7</td>
</tr>
<tr>
<td>57</td>
<td>116.3</td>
<td>99.4</td>
<td>93.3</td>
</tr>
<tr>
<td>58</td>
<td>109.2</td>
<td>102.2</td>
<td>94.6</td>
</tr>
<tr>
<td>59</td>
<td>109.7</td>
<td>104.5</td>
<td>94.8</td>
</tr>
<tr>
<td>1960</td>
<td>111.7</td>
<td>103.3</td>
<td>94.9</td>
</tr>
<tr>
<td>61</td>
<td>108.7</td>
<td>102.8</td>
<td>94.5</td>
</tr>
<tr>
<td>62</td>
<td>106.8</td>
<td>101.8</td>
<td>94.8</td>
</tr>
<tr>
<td>63</td>
<td>105.4</td>
<td>101.0</td>
<td>94.5</td>
</tr>
<tr>
<td>64</td>
<td>109.2</td>
<td>100.8</td>
<td>94.7</td>
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<tr>
<td>65</td>
<td>105.5</td>
<td>100.1</td>
<td>96.6</td>
</tr>
<tr>
<td>66</td>
<td>104.9</td>
<td>99.2</td>
<td>99.8</td>
</tr>
<tr>
<td>67</td>
<td>100.0</td>
<td>100.0</td>
<td>100.0</td>
</tr>
<tr>
<td>68</td>
<td>100.7</td>
<td>102.0</td>
<td>102.5</td>
</tr>
<tr>
<td>69</td>
<td>100.7</td>
<td>103.3</td>
<td>106.5</td>
</tr>
<tr>
<td>1970</td>
<td>99.0</td>
<td>106.6</td>
<td>110.4</td>
</tr>
<tr>
<td>71</td>
<td>96.5</td>
<td>112.2</td>
<td>113.9</td>
</tr>
<tr>
<td>72</td>
<td>96.1</td>
<td>114.9</td>
<td>119.1</td>
</tr>
<tr>
<td>73</td>
<td>101.0</td>
<td>115.4</td>
<td>134.7</td>
</tr>
<tr>
<td>74</td>
<td>110.9</td>
<td>123.1</td>
<td>160.1</td>
</tr>
<tr>
<td>75</td>
<td>114.6</td>
<td>134.2</td>
<td>174.9</td>
</tr>
<tr>
<td>76</td>
<td>117.9</td>
<td>142.2</td>
<td>182.9</td>
</tr>
<tr>
<td>1977</td>
<td>121.9</td>
<td>150.8</td>
<td>194.2</td>
</tr>
</tbody>
</table>

FIGURE 6
Types of Educational Materials Designed for Consumer Use

<table>
<thead>
<tr>
<th>Carpet/Fiber Producer</th>
<th>Educational Publication</th>
</tr>
</thead>
<tbody>
<tr>
<td>American Cyanimid Company, Fibers Division</td>
<td>&quot;A Guide to Contract Carpets&quot;</td>
</tr>
<tr>
<td>Dow Badische Company</td>
<td>&quot;An Army Could March Across a Carpet of Zefran Blend CR-4&quot;</td>
</tr>
<tr>
<td>Hercules Incorporated</td>
<td>&quot;Carpet--Symbol of Elegance&quot;</td>
</tr>
<tr>
<td>Hoechst Fibers Industries</td>
<td>&quot;How to Choose a Good Carpet&quot;</td>
</tr>
<tr>
<td>Monsanto Textiles Company</td>
<td>&quot;Acrilan Plus&quot; -- The New Excellence in Carpet Fiber</td>
</tr>
</tbody>
</table>


In addition to the publications listed in Figure 6 aimed at consumer education, some of the larger manufacturers of carpet/fiber have attempted to achieve consumer education via their advertising programs. However, this is again the exception rather than the rule within the industry. In fact, the industry as a whole does relatively little advertising. In view of the paucity of advertising efforts, the fairly small amounts of consumer education, and the numerous fibers available for producing carpet, it is hardly surprising that the consumer relies upon price as perhaps the single, most important variable in making a carpeting purchase decision. A carpet department manager for a large retail chain who asked to remain anonymous stated, "Today's consumers are very confused when they begin to purchase carpeting. I feel that my store may be making a mistake by advertising carpet at all. When you get right down to it, the only thing I have to sell
is service and price." Several similar comments were obtained in the course of the personal interviews underlying this research. The net conclusion seems to be that there is a great deal of consumer confusion about carpeting and this confusion may extend to retail store personnel. Since the last two key factors (marketing strategies and marketing segmentation) are interrelated, they will be discussed jointly at this point.

As may be surmised from the preceding comment, many firms in this industry appear to have no marketing strategy at all. Others have a marketing strategy which is only generally developed and lacks specific details. Likewise, many carpet producers have absolutely no idea of market segmentation. Instead, they judge whether they are having a good or a bad year simply by the volume of production leaving their mill. While this evaluation may be extremely myopic on the part of carpet producers, it is understandable when one examines their relationship to the consumer.

Figure 7 presents four alternative channels of distribution used in the carpet/rug industry. A producer of carpet has the alternative initially of producing for the residential market or for the contract market or both. The residential market as defined by the CRI includes purchases by a family, household or an individual for personal (non-business) use only. The contract market, on the other hand, consists of all other purchases of carpet and rugs. It is currently estimated that the contract market accounts for between 45-50% of total industry shipments and the residential market accounts for approximately 50% of total industry consumption.

A producer of carpet for the residential market has the option of selling to a distributor who in turn would sell to a retailer in order to ultimately reach the residential market. Or he may sell direct to the retailer to reach the residential market. The practice of selling direct to the
A retailer is followed mainly by producers who have contacts with retailers of sufficient size to purchase large quantities of carpet. In similar fashion, a producer of carpeting for the contract market could sell directly to contract market buyers or could sell to a distributor who would in turn sell to the contract market. Notice that in both instances where a producer is selling to the residential market, the manufacturer does not have direct contact with the consumer. Likewise, when the producer of carpeting is selling contract market products, in only one instance would the producer have direct contact with the contract market buyer. Thus, the manufacturer is often myopic about consumer needs and wants where the carpet product is concerned.

FIGURE 7
Carpet/Rug Industry -- Alternative Channels of Distribution

Further, the producer of carpet is often forced to rely upon what the retailer or what the distributor tells him regarding product needs and features. In summary, producers of carpet generally have very little consumer information upon which to base their production decisions.
Financial audits are a common occurrence in today's business world and are performed on a periodic basis with a set of standardized set of procedures and practices. So it should be with the marketing effort of firms and industries. Although a marketing audit can best be conducted on a company-by-company basis, it may be useful at this point to utilize the marketing audit concept as it might be applied to the entire carpet and rug industry. Kotler has suggested, "Every organization needs to review its basic operations from time to time to make sure they are attuned to the changing environment and opportunities. Marketing is one of the major areas where rapid obsolescence of objectives, policies, and programs is a constant possibility. First, the marketing environment tends to undergo continuous and rapid change. Second, organizational slack creeps in and afflicts all departments and renders them less than optimally efficient."

Since there is no one universal set of questions from which to develop a marketing audit, it is the opinion of the author that a relatively short but, nevertheless, critically important group of questions might serve as a starting point in performing a marketing audit on the carpet/rug industry.

Five questions form the basis for this proposed marketing audit. These are:

- Who are our customers?
- Why do they buy our products/services?
- What are we selling?
- Who is our competition?
- How do our target markets view us relative to competition?

At first glance, these five questions may seem simplistic. However, upon closer examination it will be seen that these five questions have very complex answers indeed.
Who are our customers? As was pointed out in the discussion of Figure 7, the myopic view adopted by many carpet/rug manufacturers is understandable, although very dangerous. If a carpet/rug producer views a distributor as his customer, he is being very short-sighted indeed. The "true" customer of every carpet/rug producer is the user of the carpet/rug. Thus, a carpet manufacturer who sells his product to a motel chain via a distributor could mistakenly view either the distributor or the motel chain as his customer. In fact, the ultimate customer may be the individuals patronizing the motel.

All of the basic sources of data gathered in this study lead to one inevitable conclusion regarding the answer to this question. Very little is known about the customers in the carpet/rug industry. This lack of information on the customer holds true whether we consider the contract or the residential market. An analogy may be useful to the central point we seek to make. The relationship of a carpet manufacturer to the user of a carpet is similar to the relationship between an architect and a customer or tenant in a building designed by that architect. If the architect designs a building with only the production crew in mind, he may succeed in designing a building that is easy to erect but may not be pleasing either aesthetically or functionally to the end users. So it is with carpet. A carpet/rug manufacturer can easily produce a carpet or rug which is viewed as desirable by either a distributor or a retailer. However, if this product does not meet with the residential buyer or the contract buyer's desires, the carpet/rug producer has produced an undesirable product. Thus, the answer to the question "Who is our customer?" offers a first step in attempting to provide carpet/rug manufacturers with a useful marketing strategy. Demographic information such as the age, income, education, marital status, etc. of carpet users would be very useful, especially in the residential market. Likewise, psychographic or life style
information as to the attitudes, opinions, and activities enjoyed by ultimate users would be very beneficial.

Why do our customers buy our product/service? Once having identified who the customer is, a logical progression would be to identify customer patronage motives. As covered earlier in this study, the carpet/rug industry has previously attempted to at least scratch the surface of the answer to this question. Three commercial studies have been undertaken by the carpet industry. Studies conducted in 1948, 1953, and 1961, while differing in their research design, reached the same conclusion regarding the most important factor in decisions to purchase carpeting. Color, pattern, or appearance was the single, most important factor mentioned by consumers in explaining their purchase of carpeting. While this fact provides a useful starting point in answering the question "Why do consumers purchase our product/service?", it is far from being a comprehensive answer. The studies mentioned were done over widely differing periods of time. Color preferences as well as style preferences change over period of time. Likewise, color preferences and style preferences may differ dramatically in the residential market as opposed to the contract market. Should today's carpet/rug manufacturer utilize conservative or non-conservative colors in the production of carpet? Should the texture of carpets be more contemporary or traditional? These are but a few of the areas that must be explored in order to gain answers to this second question.

What are we selling? Earlier in this report, the extensive use of price in advertising has been documented. A carpet/rug producer must objectively and introspectively ask himself this question "What am I selling?" If the answer to the second question is known, that is if we understand why customers buy our products or services, then we should be in a position to complement that in terms of the factors we emphasize in marketing our products. Does carpeting represent only a way to cover an otherwise bare floor? Does
carpeting represent an extension of one's life style or personality? Does carpeting add warmth to a room? These are but a few of the areas that must be explored in attempting to answer this third question. However, it is important to reflect upon the comments made earlier regarding the extensive use of price as well as the general lack of industry consumer education attempts. The carpet/rug industry may well have been selling an undifferentiated product and emphasizing price alone in its previous promotional efforts. Any marketing audit which did not strongly suggest that the industry needs to take a very strong and objective look at the answer to this question would be less than candid.

Who are our competitors? The vast majority of carpet/rug producers in Federal Region IV view the other carpet producers residing in this region as their competition. This is short-sighted. Enlarging this definition of competition to include all U.S. producers of rugs/carpeting would still be short-sighted. In this era of international trade, all carpet/rug producers would represent the starting point in defining competition. Through the Carpet and Rug Institute, statistics have been attained on the volume of carpeting and rugs imported into this country. These are presented in Figure 8.

As may be seen from an analysis of statistics in Figure 8, the dollar volume of imports in 1977 represents a 22% increase over the dollar volume imported in 1976. Thus, foreign carpet/rug producers must be considered when defining competition. However, this is only a starting point. Additionally, producers in this industry must consider as competition manufacturers of paint products, wall murals, wall coverings, mirror tile, cork tile, etc. The point we seek to make here is that competition must be defined very broadly and the advantages and disadvantages of carpeting must be considered in this broader context of competition.
The other side of the competitive coin concerns the product of American producers when it is exported to foreign markets. Figure 9 presents statistics on exports of carpeting and rugs.

An analysis of Figure 9 indicates that the dollar volume of 1977 exports of carpet and rugs increased by only 3% over the dollar volume exported in 1976. Carpet and rug producers located in Federal Region IV may have substantially different competitors when they elect to export their product abroad.

How do our target markets view us relative to competition? The critical words in this question are the words "relative to." It is important for any manufacturer not to examine his product or service in isolation, but to attempt to view it as hig target market might view it in light of competition.
Thus, the carpet/rug producer located in Federal Region IV must look beyond the information provided by their own quality control/production department.

**FIGURE 9**

Exports of Carpet and Rugs By Type (ooo’s Omitted)

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Hand-Made Orientals</td>
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<td>1,340</td>
<td>1,007</td>
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<td>Wilton &amp; Velvet</td>
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<td>1,509</td>
<td>1,837</td>
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<td>Other Woven</td>
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<td>3,396</td>
<td>2,458</td>
<td>3,247</td>
<td>2,986</td>
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<tr>
<td>Tufted</td>
<td>570</td>
<td>322</td>
<td>351</td>
<td>848</td>
<td>1,151</td>
</tr>
<tr>
<td>Braided**</td>
<td>6,141</td>
<td>3,842</td>
<td>3,366</td>
<td>4,393</td>
<td>3,735</td>
</tr>
<tr>
<td>All Other</td>
<td>2,269</td>
<td>2,154</td>
<td>2,050</td>
<td>2,432</td>
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<td>TOTAL IMPORTS</td>
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<td>12,378</td>
<td>10,751</td>
<td>13,988</td>
<td>13,871</td>
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</table>

<table>
<thead>
<tr>
<th>Dollar Value*</th>
<th></th>
<th></th>
<th></th>
<th></th>
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</thead>
<tbody>
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<td>Hand-Made Orientals</td>
<td>$ 35,948</td>
<td>$ 42,897</td>
<td>$ 35,841</td>
<td>$ 50,110</td>
<td>$ 64,685</td>
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<tr>
<td>Wilton &amp; Velvet</td>
<td>12,048</td>
<td>11,086</td>
<td>12,559</td>
<td>17,273</td>
<td>21,965</td>
</tr>
<tr>
<td>Other Woven</td>
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<td>21,687</td>
<td>19,182</td>
<td>24,166</td>
<td>23,064</td>
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<tr>
<td>Tufted</td>
<td>5,882</td>
<td>4,846</td>
<td>4,169</td>
<td>7,125</td>
<td>9,004</td>
</tr>
<tr>
<td>Braided**</td>
<td>10,923</td>
<td>7,775</td>
<td>6,757</td>
<td>9,954</td>
<td>9,552</td>
</tr>
<tr>
<td>All Other</td>
<td>8,145</td>
<td>9,698</td>
<td>8,784</td>
<td>11,077</td>
<td>13,049</td>
</tr>
<tr>
<td>TOTAL IMPORTS</td>
<td>$ 97,027</td>
<td>$ 97,989</td>
<td>$ 87,292</td>
<td>$119,705</td>
<td>$146,319</td>
</tr>
</tbody>
</table>


Their output must be seen as the potential consumer would see it. Does it compare favorably with the products of competition as we have defined competition in the preceding question? Does the carpet/rug produced compare favorably with non-carpet/rug forms of competition, such as wall coverings, paint, mirror tile, etc?
Clearly, the five questions which have been enumerated represent only a starting point in doing a marketing audit. Nevertheless, this industry desperately needs to conduct such an audit in order to better ascertain where it is and where it is headed. It is only through providing detailed and objective answers to these questions that the industry may seek to develop a comprehensive and effective marketing strategy for its products.

3. RECOMMENDATIONS FOR CHANGE

The two preceding sections of this paper have sought to provide historical background on the carpet industry in Federal Region IV as well as to provide information regarding the current marketing practices of the industry. This section provides recommendations for changes if the industry wishes to develop a more viable marketing strategy.

Significant Issues

The five questions concluding the previous section provide a basis for beginning development of a marketing strategy. Collectively, the limited data available to answer these five questions should be disturbing to members of the industry. Little is known about customers and competition. However, enough is known concerning each of these issues to provide some specific recommendations for change.

Specific Recommendations for Enhancing Marketing Practices

A first recommendation emerging from this research is that the carpet industry must do something to increase its future potential. The "something" to be done could include one of several options. First, develop new products such as the artificial grass carpeting which has recently been developed in the industry. This new product has significant new and alternative uses over existing carpet products since it may be used outdoors, around
swimming pools, etc. Further, developments of this type may be one possible solution. A second approach would be to develop new markets. Collectively, the carpet/rug producers in Federal Region IV have done little to explore foreign markets. The Carpet and Rug Institute Incorporated has recently formed an organization which would specifically deal with this foreign market potential. Known as the International Carpet and Rug Market (ICRM), this organization will sponsor the first international carpet and rug market held in the United States. Scheduled for July 13-16, 1980 in Atlanta, this exhibit is anticipated to attract over 200 exhibitors representing all segments of the U.S. carpet and rug industry.

Yet another method for enhancing industry potential is to further increase the sale and use of carpet in areas currently dominated by competition. An entire spectrum of the market, for example, uses hard-surface, floor covering in lieu of carpeting. The work of Lanzillotti (1955) provides an excellent starting point in defining the hard-surface competition faced by the carpet/rug industry.

A second recommendation for enhancing marketing practices is additional and sorely needed consumer education. The carpet/rug industry must attempt to educate middlemen if it hopes to educate the consumer. Thus, retail sales persons as well as the sales personnel employed by the distributors must be well educated on technical aspects of carpeting if they wish in turn to educate the consumer. Additional attempts at consumer education can be achieved both through advertising and the types of consumer education mentioned in Figure 6. The Carpet and Rug Institute currently offers a product training school which may be attended either by retail or distributor sales personnel. Additional efforts of this type are needed if the industry is to make sufficient progress in educating both middlemen and consumers of
carpeting products.

A third and final recommendation for enhancing marketing practices is that the industry must seek to obtain further product differentiation. This industry can no longer afford the luxury of an undifferentiated product. In the past, growth in the housing market has provided a dramatic increase in the residential segment for rug/carpet products. Likewise, in the recent past, the contract market has increased due to spiraling construction. If this industry is to grow and survive, specific marketing strategies to establish product differentiation must be pursued.
REFERENCES


FOOTNOTES

SMALL BUSINESS' ROLE IN THE
FURNITURE INDUSTRY OF THE SOUTHEAST

James E. Littlefield
University of North Carolina at Chapel Hill

1. SUMMARY

The number of small businesses manufacturing wooden and upholstered furniture has increased significantly in the Southeast in the 1970's. There are many indications that the market for both wooded and upholstered furniture in the United States will be even more favorable throughout the 1980's, and thus many more furniture manufacturing entrepreneurs will probably be induced to enter the competitive market.

History has shown that many small businesses have come into being under favorable market conditions and have subsequently failed during times of cyclical economic down-turn, due to shortcomings in the areas of management expertise, marketing, finance, and accounting. Procedures are outlined in this paper which will help the potential SBA loan applicant to overcome these pitfalls.

Finally, recommendations are made which are intended to improve the effectiveness of the SBA loan-granting process and concerning the nature of consulting assistance which the government may render to a new or troubled small furniture manufacturer.

2. INTRODUCTION

The purpose of this paper is to develop a perspective for the role of small business in the furniture industry in the Southeast.

The Southeast is not a particularly precise geographical designation, but at least for the furniture industry, its center is North Carolina and Virginia, and includes at least the following other states: Alabama, Georgia,
Florida, Mississippi, South Carolina, and Tennessee.

The references at the end of this paper are those which pertain to small businesses or those which are the most comprehensive. Many other references were consulted, particularly those in the business press, but they were not particularly helpful and are too numerous to mention.

A number of people helped with this paper and thanks are due to them. Among them were Mr. Douglas Kerr, Executive Vice President of the Southern Furniture Manufacturers Association in High Point; Mr. Dan Kirkendahl, Vice President, Governmental Affairs, of SFMA's Washington office; Mr. David J. Brunn of Chapel Hill; Mr. Ben Jarnigan of Bean Station, Tennessee; Mr. Fred Council of Denton, North Carolina; Mr. Jerry H. Fox of Raleigh; Mr. Ken Campbell of High Point; and Mr. Joe Lawless of the U.S. Department of Commerce, Washington. Messrs. Michael Jacobs and Nick Williamson helped with research and editing for the project.

For this paper, small business will be defined as enterprises with less than twenty employees. Not only does this make sense from the standpoint of the furniture industry, because many of its firms have fewer than twenty employees, but also, Bureau of the Census statistics are collected on this basis.

The furniture industry can be divided in a number of ways. Household furniture and office furniture is a logical division. The household sector is the larger of the two, and most of this paper will deal with this sector. A summary profile is provided in Table 1.

3. HISTORY OF FURNITURE MANUFACTURING IN THE SOUTHEAST

The furniture industry in the Southeast started in about the 1880's predominantly in Virginia, Georgia, and Tennessee. North Carolina's start in this industry was first noticed when the U.S. Census counted six factories
### TABLE 1
1978 PROFILE
HOUSEHOLD FURNITURE

<table>
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<th>SIC CODE: 251</th>
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</table>

| Value of shipments (million $) | 10,681 |
| Value added by manufacture (million $) | 5,550 |
| Total employment (000) | 320 |
| Number of establishments (1972) | 5,370 |
| Number of companies (1972) | 4,927 |
| Exports as a percent of product shipments | 1 |
| Imports as a percent of apparent consumption\(^1\) | 5 |
| Compound annual rate of change, 1973-78: |
| Value of product shipments | 4.7 |
| Value of exports | 23.2 |
| Value of imports\(^2\) | 14.9 |
| Total employment | -0.4 |

**Major producing regions (or States):** North Carolina, California, Virginia, New York, Tennessee, Pennsylvania, Indiana, and Illinois.

\(^1\) Imports divided by product shipments plus imports minus exports.

\(^2\) Rates of change based on current dollars.

**Source:** Bureau of the Census; Bureau of Labor Statistics; Industry and Trade Administration (BDBI) estimates.

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in 1890. From this modest start, North Carolina has developed into the state with the largest furniture production in the nation. In terms of furniture establishments, North Carolina is far in the lead with 286 establishments in 1977, followed by Tennessee with 106, Mississippi with 65, and Florida with 42. These numbers may be found in Table 4, later in this paper.

The major impetus for the Southeast to become a factor in the industry, and for its subsequent growth, was consumer acceptance of furniture of veneered, rather than solid construction, and the abundance of woods, particularly poplar and gum, in the Appalachian range. These woods were used for "core stock" in veneered panels for the construction of tops, end panels, drawers and drawer fronts, and to build relatively inexpensive furniture. Although these
woods continue to be used, technology has provided many wood substitutes, such as particle board, plastics, and "engraved" veneers.

Another impetus for the development of the industry in the Southeast was the need for a marketing center. Because of the virtual impossibility of transporting furniture samples over long distances, it became necessary to have a central place for retailers to view furniture for which they would immediately or ultimately place orders, hence; the development of the furniture market center, first in Jamestown, New York and New York City near the turn of the century, then in Chicago and Grand Rapids, and ultimately in the High Point area. Although other regional furniture markets remain, the "Southern" market, centered in High Point but with Manufacturer showrooms located also in nearby cities, including Hickory and Lenoir, is the largest and strongest of them all. There are frequent and pervasive calls for and predictions of the demise of the furniture market system. None of these seem to dampen the ardor of retailers or manufacturers.

To the factors of wood availability and the market system must be added the relatively low wages in the Southeast to account for the furniture industry's establishment and growth there.

**Employment and Production Trends**

Table 2 reviews the economic progress of the household furniture industry from 1973 through the forecast for 1979. The two divisions in the table are:

1. **Industry**—the value of the products and services sold by the industry, and
2. **Product**—the value of the product shipments. The key point differentiating these two items seems to be that the industry figure includes services as well as products.
The largest growth during 1973-79 has been in wood furniture, a 58% increase for products and services and a 43% increase for products alone. Overall, household furniture shipments increased nearly 40% during the 1973-79 period.

Total employment decreased slightly between 1973 and 1978, reaching an extremely low level in 1975, nearly 19% less than in 1973. This decrease was due to the 1974 recession, which affected household furniture sales very strongly. Employment has also been affected, in part by the continued increase in the use of labor-saving devices. As wages (see average hourly earnings in Table 2) have risen in the industry, automation has become more practical.

**Future of the Industry**

In spite of the less than spectacular statistics for the 1973-79 period, the industry has good reason to look forward to steady growth in the years to come. This is especially true for better-quality merchandise. Medium- to high-priced furniture is currently showing, and is expected to continue to show, better sales strength than the lower-priced lines. This information and the following statement come from a report on the furniture industry by W. W. Epperson of Wheat, First Securities, Inc., August 4, 1976: "The post-war baby boom continues to stimulate furniture sales as the 18-34 age group (prime furniture buyers) continues to grow. In 1960, this group had 39 million individuals; by 1980 it will surpass 65 million persons."

Other growth factors noted by Wheat, First Securities, Inc. include the overall continued growth in the U.S. population, the ability of the family unit to afford new home furnishings because of the continued increase in the number of working wives, the continued increase in discretionary income, and the continuing high level of mobility in the population, especially among the more quality-conscious 35-44 group.
## Table 2

### Household Furniture: Trends and Projections 1973-79

(In millions of current dollars except as noted)

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</thead>
<tbody>
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<td>Value of shipments</td>
<td>8,217</td>
<td>8,365</td>
<td>7,770</td>
<td>9,041</td>
<td>9,748</td>
<td>10,681</td>
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<td>Wood (2511)</td>
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<td>3,095</td>
<td>3,780</td>
<td>4,195</td>
<td>4,700</td>
<td>5,075</td>
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<td>310</td>
<td>325</td>
<td>335</td>
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<td>Household Furniture, n.e.c. (2519)</td>
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<td>179</td>
<td>198</td>
<td>214</td>
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<td>4,998</td>
<td>5,550</td>
<td>5,550</td>
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<td>Value added per production worker-hour ($)</td>
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<td>266</td>
<td>303</td>
<td>320</td>
<td>346</td>
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<td>226</td>
<td>267</td>
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<td>Percent change in average hourly earnings (year to year)</td>
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<td>Value of shipments</td>
<td>7,986</td>
<td>7,957</td>
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<td>10,053</td>
<td>10,715</td>
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<td>Wood (2511)</td>
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<td>1,380</td>
<td>1,450</td>
<td>5</td>
<td>21</td>
<td></td>
</tr>
<tr>
<td>Wood TV/Radio Cabinets (2517)</td>
<td>275</td>
<td>312</td>
<td>261</td>
<td>315</td>
<td>355</td>
<td>365</td>
<td>365</td>
<td>3</td>
<td>23</td>
<td></td>
</tr>
<tr>
<td>Household Furniture, n.e.c. (2519)</td>
<td>250</td>
<td>240</td>
<td>213</td>
<td>236</td>
<td>257</td>
<td>273</td>
<td>305</td>
<td>8</td>
<td>22</td>
<td></td>
</tr>
<tr>
<td>Producer price index (Dec.)</td>
<td>107.3</td>
<td>122.0</td>
<td>126.2</td>
<td>133.8</td>
<td>140.4</td>
<td>150.2</td>
<td>178.0</td>
<td>2</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Percent change in producers price index (Dec. to Dec.)</td>
<td>7</td>
<td>14</td>
<td>4</td>
<td>6</td>
<td>5</td>
<td>4</td>
<td>7</td>
<td>2</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Trade</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Value of exports</td>
<td>49</td>
<td>79</td>
<td>84</td>
<td>126</td>
<td>136</td>
<td>139</td>
<td>19</td>
<td>2</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Value of imports</td>
<td>278</td>
<td>303</td>
<td>260</td>
<td>364</td>
<td>464</td>
<td>557</td>
<td>557</td>
<td>20</td>
<td>-</td>
<td></td>
</tr>
</tbody>
</table>

1. Value of all products and services sold by the household furniture industry (SIC 251).
2. Estimated except for hourly earnings, price indexes and 1977 trade data.
3. As of May 1978.
4. December 1977 to December 1978
5. 1967 is base period for the industry price index; 1972 for the producers price index.
6. Value of shipments of household furniture produced by all industries.
7. Forecast.

N.E.C. - Not elsewhere classified. Total may not add due to rounding.

Business Week magazine, July 30, 1979, notes yet another reason for industry optimism: uncertainty over availability of gasoline and its soaring price will redirect much of people's leisure time to activities at home.

In short, the furniture industry is expected to continue its cyclical and volatile nature, but secular trends promise a steady and healthy upward trend. Some industry observers predict 1980-1990 to be the best ten years of this century for the industry.

4. SMALL BUSINESSES' ROLE IN THE FURNITURE INDUSTRY

Data for this section of the paper are scarce. Few statistics are available for small firms. The only statistical source found is the U.S. Census of Manufactures. Other information was obtained over the telephone from industry and government sources.

The 1977 Census of Manufactures gives the information in Table 3 on the number of establishments in Upholstered Household Furniture (SIC Code 2512). The total number of firms declined between 1958 and 1972, but the 1977 Census reports an increase in the number of these firms. The number of smaller firms, those with less than 20 employees, declined as well between 1958 and 1972, but both the number and percentage of small firms increased in 1977. This indicates that the firms dropping out of the industry during bad times, and those starting in business during good times, are smaller firms. The reader should remember that these are national statistics.

Some of the same statistics are available for regions of the U.S.; an increase in numbers of upholstered household furniture establishments was registered as well in the Southeast between 1972 and 1977. Table 4 illustrates these figures. Of the eight states under study, only Georgia did not show an increase in number of establishments during this period. The overall increase in the Southeastern Region was 22%, but this increase varied from 55% in
TABLE 3

U.S. UPHOLSTERED HOUSEHOLD FURNITURE ESTABLISHMENTS

SIC CODE 2512

<table>
<thead>
<tr>
<th>Census year</th>
<th>Establishments with 20 or more employees</th>
<th>% of Total</th>
<th>Establishments with 19 or less employees</th>
<th>% of Total</th>
<th>Total establishments</th>
</tr>
</thead>
<tbody>
<tr>
<td>1958</td>
<td>682</td>
<td>39</td>
<td>1078</td>
<td>61</td>
<td>1760</td>
</tr>
<tr>
<td>1963</td>
<td>712</td>
<td>40</td>
<td>1073</td>
<td>60</td>
<td>1785</td>
</tr>
<tr>
<td>1967</td>
<td>727</td>
<td>44</td>
<td>917</td>
<td>54</td>
<td>1644</td>
</tr>
<tr>
<td>1972</td>
<td>770</td>
<td>59</td>
<td>537</td>
<td>41</td>
<td>1307</td>
</tr>
<tr>
<td>1977</td>
<td>725</td>
<td>49</td>
<td>742</td>
<td>51</td>
<td>1467</td>
</tr>
</tbody>
</table>


Mississippi to a 4% loss in Georgia.

A consideration of the percentages of firms in the region and each state with less than 20 employees indicates a trend similar to that experienced in the nation. Whereas between 1972 and 1977, the percentage of "small" upholstery firms in the nation increased from 41% to 51%, in the Southeastern Region it increased from 32% to 41%.

Also from the 1977 Census of Manufactures are the data in Table 5, showing the number of firms in 1972 and 1977 for Wood Household Furniture (SIC 2511). In total, wood household furniture producers increased by 26% between 1972 and 1977. However, whereas those firms with less than 20 employees increased 42%, those with 20 or more employees decreased by 2.5%. It is clear that small firms have found the wooden household furniture industry of interest in recent years. As with the numbers for Upholstered Household Furniture, these are national figures.
<table>
<thead>
<tr>
<th>South Atlantic Division</th>
<th>1977</th>
<th>1972</th>
<th>Percent Increase in Total Establishments 1977 vs 1972</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Establishments</td>
<td>Establishments with 20 or</td>
<td>Establishments with 19 or</td>
</tr>
<tr>
<td></td>
<td>with 20 or more employees</td>
<td>more employees</td>
<td>less employees</td>
</tr>
<tr>
<td></td>
<td>with 19 or less employees</td>
<td>more employees</td>
<td>Establishments with 20 or</td>
</tr>
<tr>
<td></td>
<td>% of Total</td>
<td>% of Total</td>
<td>Total Establishments</td>
</tr>
<tr>
<td>Virginia</td>
<td>24</td>
<td>16</td>
<td>67%</td>
</tr>
<tr>
<td>North Carolina</td>
<td>286</td>
<td>180</td>
<td>63%</td>
</tr>
<tr>
<td>South Carolina</td>
<td>9</td>
<td>5</td>
<td>56%</td>
</tr>
<tr>
<td>Georgia</td>
<td>21</td>
<td>12</td>
<td>57%</td>
</tr>
<tr>
<td>Florida</td>
<td>42</td>
<td>14</td>
<td>33%</td>
</tr>
<tr>
<td>TOTAL DIVISION</td>
<td>382</td>
<td>227</td>
<td>59%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>East South Central Division</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tennessee</td>
</tr>
<tr>
<td>Alabama</td>
</tr>
<tr>
<td>Mississippi</td>
</tr>
<tr>
<td>TOTAL DIVISION</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>TOTAL SOUTHEASTERN REGION</th>
</tr>
</thead>
<tbody>
<tr>
<td>582</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Establishments</th>
<th>Establishments with 20 or more employees</th>
<th>Establishments with 19 or less employees</th>
<th>Percent Increase in Total Establishments 1977 vs 1972</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>% of Total</td>
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<td>Establishments with 19 or less employees</td>
</tr>
<tr>
<td>Virginia</td>
<td>24</td>
<td>16</td>
<td>67%</td>
</tr>
<tr>
<td>North Carolina</td>
<td>286</td>
<td>180</td>
<td>63%</td>
</tr>
<tr>
<td>South Carolina</td>
<td>9</td>
<td>5</td>
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<tr>
<td>Georgia</td>
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<td>12</td>
<td>57%</td>
</tr>
<tr>
<td>Florida</td>
<td>42</td>
<td>14</td>
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<tr>
<td>Mississippi</td>
</tr>
<tr>
<td>TOTAL DIVISION</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>TOTAL SOUTHEASTERN REGION</th>
</tr>
</thead>
<tbody>
<tr>
<td>582</td>
</tr>
</tbody>
</table>

Establishments with Census 20 or more year employees employees
1972 827 20 or more 35 % of total employees
1977 806 20 or more 27 % of total employees

% Increase (Decrease)
1972-77 (2.5) 42 % of Total establishments

Table 5 presents the number of firms in each of the states of the Southeastern Region. Several items of interest may be found in these data.

First, the Region's total number of firms increased only eight percent. Most of this increase came about in the East South Central Division, most especially Mississippi, which had a 100% increase in the number of firms between 1972 and 1977.

Within the South Atlantic Division, North Carolina had a good increase, 24%, but the other three states had no gain or a loss in the number of firms. Florida had a 46% decrease in firms.

It is clear that small firms are alive and well in the furniture industry in the Southeastern Region. However, the healthiest growth in numbers of firms is in Mississippi, North Carolina, Tennessee, and Virginia.

Problems of Small Business in the Industry

If cash flow is a problem for a large business, it becomes an even more difficult problem for a small business with less flexibility and resources. However, even though the problems of small businesses are somewhat universal,
TABLE
WOOD HOUSEHOLD FURNITURE ESTABLISHMENTS BY REGION
SIG Code 2511

<table>
<thead>
<tr>
<th>South Atlantic Division</th>
<th>1977</th>
<th>1972</th>
<th>Percent Increase (Decrease) in Total Establishments 1977 vs. 1972</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Total Establishments</td>
<td>Establishments with 20 or more employees</td>
<td>% of Total</td>
</tr>
<tr>
<td>Virginia</td>
<td>67</td>
<td>37</td>
<td>55%</td>
</tr>
<tr>
<td>North Carolina</td>
<td>215</td>
<td>121</td>
<td>56%</td>
</tr>
<tr>
<td>South Carolina</td>
<td>21</td>
<td>9</td>
<td>43%</td>
</tr>
<tr>
<td>Georgia</td>
<td>78</td>
<td>26</td>
<td>33%</td>
</tr>
<tr>
<td>Florida</td>
<td>88</td>
<td>21</td>
<td>24%</td>
</tr>
<tr>
<td>TOTAL DIVISION</td>
<td>469</td>
<td>214</td>
<td>46%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>East South Central Division</th>
<th>1977</th>
<th>1972</th>
<th>Percent Increase (Decrease) in Total Establishments 1977 vs. 1972</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tennessee</td>
<td>114</td>
<td>29</td>
<td>25%</td>
</tr>
<tr>
<td>Alabama</td>
<td>66</td>
<td>16</td>
<td>24%</td>
</tr>
<tr>
<td>Mississippi</td>
<td>56</td>
<td>14</td>
<td>25%</td>
</tr>
<tr>
<td>TOTAL DIVISION</td>
<td>236</td>
<td>59</td>
<td>25%</td>
</tr>
<tr>
<td>TOTAL SOUTHEASTERN REGION</td>
<td>705</td>
<td>273</td>
<td>39%</td>
</tr>
</tbody>
</table>

that makes them no less real and in need of solutions.

The problems of small businesses in the furniture industry reviewed here are those discussed in interviews with the people mentioned in the introduction of this paper. A number of problems were mentioned, with a great deal of overlap in the discussion. Those problems reviewed below were mentioned by several people, and are presented in general to specific order, not necessarily in order of importance.

Management expertise. Most new, small businesspeople know little or nothing at the start about how to manage a total business. The scenario described by one of the people interviewed went as follows:

A shop foreman or lower level executive of a relatively large upholstery manufacturer decides to strike out on his own. He teams up with a sales representative who has a developed relationship with a large store or chain. Together they see an opportunity to reproduce, at a lower price level, one of the lines sold by Drexel, Henredon, or one of the other larger upholstery producers. The store welcomes this new firm and gives it a substantial amount of business because it sees an opportunity to get almost the same merchandise at a lower price and to control distribution in its trading area. Thus, the new firm has little trouble reaching a one-half million or even a million dollar sales level.

However, as the firm's sales level increases, management problems crop up. Although the investment in upholstery manufacturing is small, money is needed for some equipment, for establishing a factory, for payrolls, for work-in-process inventory, and for other items. Almost immediately the firm is in financial difficulty. If the store which is the major customer is a slow payer, the financial problems are magnified.

Another almost immediate problem is the lack of appropriate systems and procedures in the manufacturing process or office. Records are not
kept accurately, so the firm does not have a good notion of its costs or inventories. Because the store is actually setting the price, it is easy for the firm to have its costs outweigh its revenues.

Other problems arise to jeopardize the firm's future. Included in these are such diverse items as dealing with banks, factoring firms, and other financial institutions; supervision problems; dealing with OSHA, CPSC, and other local, state, and national governmental agencies and regulations; marketing problems in expanding the customer base; and many others.

The point here is that management expertise is lacking in many small businesses. If this void is not soon overcome, the business does not long survive. The scenario described here is most prevalent in upholstered household furniture, which is easier to enter, but is true also, to a lesser extent, in case goods, wooden furniture.

Marketing. On a narrower scale, a major problem of small businesses in the furniture industry is the lack of marketing expertise. The major impetus for starting the new, small business most often comes from a person knowledgeable about manufacturing. His knowledge of the household furniture distribution system, of promotion, of pricing, usually is small or nonexistent. As a result, many marketing mistakes will be made, especially in the early stages of the firm's development.

Particularly important and lacking is an analysis of distribution channels. Instead of considering all the alternative channels: "contract" to retail chains only, selling only to wholesalers, using commission representatives, "selling direct to everyone," among others, and choosing the best channel, many small firms will enter an unknown and unresearched channel and will find a considerable amount of competition they did not know existed.
Finance. As mentioned earlier, finance is a major early problem for most small businesses. Dealing with banks and factoring firms is usually time consuming and expensive. The small firm turns to a factor in order to get his accounts receivable turned into cash more quickly, and although he does get money quickly, he still retains the risk of nonpayment. The small firm will more often sell to accounts with less than ideal credit ratings, and often this type of firm will either not pay or will pay slowly. In addition, "borrowing" from a factor often is very expensive for manufacturers.

Cash flow projections are a major problem for many small manufacturers. Such businesses sometimes find themselves "cash rich," but perhaps more often they are "cash poor," resulting in slow paying of suppliers and questionable credit ratings.

Inventory Control Systems. Most small furniture manufacturers have a great problem of having raw materials in proper balance so that they may deliver orders reasonably quickly yet not have excessively expensive levels of raw materials on hand at all times. Firms, many of them small, which order frames and fabric only after receiving an order are bound to have delivery, customer satisfaction, and financial problems.

Government regulations seem to be more of a burden for small businesses in the industry than for larger ones. First, the firm, with its limited management, finds it difficult to know which regulations apply to it and how they apply. Second, the firm has problems in acquiring the technology to conform to the regulations. Many of the regulations have to do with acquiring health or safety devices or equipment. These devices or equipment may require a high level of investment and technical expertise, both of which are difficult to obtain. After acquiring the technology and necessary devices, of course, it then becomes a problem to train management and employees to use and maintain the new equipment.
Incidentally, interviewees reported that many smaller firms simply ignore government regulations until they are "caught." Then the cost and speed necessary to conform to the regulations often is greater. One respondent estimated that 50% of the regulation nonconformance is due to ignorance and 50% is willful.

The general area of recordkeeping is another problem for small operators. Bookkeeping skills are generally scarce and willingness to keep good records is lacking. These are usually people of "action," not people willing to sit behind a desk for periods of time or people willing to supervise office employees.

Thus, small firms in the furniture industry have many problems, causing high turnover of firms, much loss of financial and human capital, and a general inefficiency in the industry resulting in consumer dissatisfaction and bad public relations. However, government policy makers have an opportunity to correct the climate which allows these problems to exist. Suggestions for policy changes will be made in the next section.

5. RECOMMENDATIONS FOR IMPROVING SMALL BUSINESS INVOLVEMENT IN THE FURNITURE INDUSTRY

The recommendations below will be discussed as if any or several government agencies could consider policy changes, with the exception of those addressed specifically to the Small Business Administration.

Consulting help in greater amounts and with better quality could be provided to small producers in the furniture industry. This would entail first getting consultants with practical industry knowledge, not just people with technical expertise in accounting, marketing, finance, or some other specialized area. Second, it would entail sending in fewer people. One interviewee stated: "Government agencies want to send in ten people (presumably specialists) instead of one, good, all-around consultant." This consultant, or at most two or three consultants then would help the firm in at least the
following areas, staying around until some results are shown:

a. Explain long-range planning and help write such a plan for the firm.

b. Explain and help develop manufacturing and office systems and procedures, including accounting and other record keeping.

c. Explain the basics of cash flow and money management and help install a money management system.

d. Help with hiring and organization development problems.

Information on the sources of both SBA and other government assistance which is available to small businesses would be helpful. Included in this recommendation is a need for more, clearer information on just what sort of business and person is eligible for an SBA loan. There is a perception among at least some businesspeople that the SBA exists mostly to loan money to minority busineses. This misperception should be corrected by publicity and action.

Along these same lines, apparently at least some banks need to be sold on the concept of SBA-guaranteed loans. Some interviewees report that banks discourage applications from businesses which should be eligible to apply.

The SBA should develop better criteria for deciding who should get loan guarantees. Put in the right hands, of course, a loan guarantee will help a business be more successful. Interviewees perceive that loan guarantees are often not given to the best businesspeople. Often, guarantees are given to those who can best "fill out the forms;" the SBA can be faster in responding to loan guarantee requests. Paper work takes time, but many businesspeople believe that the sometimes excessive duration of the wait for an SBA approval in itself helps doom the small business.

Applications for SBA guaranteed loans could be improved. It is more likely that the correct firms and people would then be granted loans. Such
application improvements would include:

a. A well-thought-out marketing plan with an outline of the market segment or segments to be developed, an analysis of which retailers or other intermediaries will be used (rather than just one large customer), a logical pricing structure, and an overall promotion program.

b. A cost and budgeting system which will allow for profitable operation.

c. In short, evidence that the firm will be more than just a "me too" operation with no significant rationale for existence.

Tax and regulation considerations for an initial period would help small businesses. If a moratorium on certain taxes and regulations for a two-to three-year period could be granted, many small firms which now are falling by the wayside could make it through the hardest times until they become stronger in financial and management resources.
REFERENCES

1. Raymond A. Helmers, "Exclusive Interview with 'Mr. Furniture,'" Henry A. Foscue, Furniture Manufacturing Management, Vol. 25, No. 4, April, 1979, pp. 18-22.


1. INTRODUCTION

To address the role of agribusiness from a meaningful perspective, it is necessary to set the stage internationally, then describe American developments, and then point out the regional perspective. This is because agriculture has grown from a system of local, small, self-sufficient farmers, to one of large corporate-owned or independent farms, which in combination with processing and marketing organizations cause nationwide and international impact. Thus, a brief history is provided which explains the role changes that have taken place, and the development of the various subsectors of agribusiness over life cycles to reach maturity. This report then presents a current status of agribusiness in the southeast and concludes with implications for small business.

This report depends heavily on personal contacts and phone interviews by the author. In addition, the general framework comes from experience of the author who from 1947 through 1967 was employed in agribusiness industry and participated in the transfer of technology into the southeastern United States and internationally.

2. ROLE AND DEVELOPMENT OF AGRIBUSINESS

Much has been written in the past 25 years about innovation and adaptation of technology in agriculture, both in the United States and in developing nations. Similarly, volumes have been written about industrial
technology and productivity, and about economic development built around national and international policy, again in the United States and in developing nations. And volumes can be read about political history and international trade beginning with Asian and Middle-Eastern traders, European empires, and most recently about the multi-national corporations. The questionable value of foreign policies and programs of all nations which have led to the rich countries getting richer and the poor countries remaining poor have been reported, sometimes with considerable disdain. In the U.S.A., a long-standing debate centers around government policies that have lead agriculture to be, by some definitions, a very large "utility." Some clamor for more deregulation. The pricing of products in most subsectors has long since left the purely competitive model of economics. Administered pricing and contract production are common practice today.

That agriculture in America is one of the most, if not the most, technologically advanced in the world is well documented. The pattern of world grain trade has shifted almost entirely in favor of the developed nations; and for 1976 show North America the leading net exporter of 94 million metric tons, with Australia and New Zealand second with 8! Not only have nearly all countries become food importers, but a growing number now import over half their grain supplies (Brown, 1976).

Lester Brown, in his article "The Limits to Growth of Third World Cities," makes the point that third world cities are reaching their limits to growth because the rural-to-urban exodus is limiting food production and labor supplies, and at the same time increasing purchased-food and purchased-energy requirements.

As Professor Earl O. Heady states of American agriculture, "Its high productivity is a result of two centuries of development policy, low prices of land and other things needed for farming, stable prices for farm products, and
the promotion of innovation" (Heady, 1976).

Briefly, the four stages of agricultural growth are as follows. The first, according to Hopper (1976), is traditional farming whereby the farmer is self-sufficient and dependent entirely on the natural elements of rain, sun, etc. The second stage utilizes irrigation and drainage technology to improve productivity. The third stage uses more scientifically-developed technology, such as special varieties of plants on irrigated land with fertilizer or the use of vaccines and dips to control livestock disease. The fourth stage is that of high-productivity agriculture built on technology and a full range of institutions and infrastructure. The main emphasis in these stages of development over time is not on marketing, but on the improvement of production techniques—better seeds, more resistant varieties, hybrid vigor, faster growth, more uniform output. As the stages progress, labor migrates to the cities and becomes part of the market. In the United States, the labor migration away from the farm took place for two reasons: low income during the economic depressions of the early 1900's, and the personal desire of individuals for non-farm work. Following World Wars I and II, the emerging markets opened opportunities for more mechanization and innovation.

It now appears that if more of the infrastructure and supporting small institutions can be located away from the large metropolitan areas, labor can be encouraged to remain in the rural areas where small farms, firms, and family-sufficiency prevail. Hopefully, there would be a decrease in the exodus to the large cities where slums, poverty, unemployment, and political unrest develop. The labor for manufacturing can remain in the rural areas. In the U.S. model, industry had to locate in the urban areas because that is where the unemployed labor supply and transportation (railroads) had already located. In recent years, however, American meat processors, poultry processors, and vegetable processors are moving out of the large urban areas where they have high-cost
labor and congested transportation, and they are going back to the farming areas. One development that has facilitated this is the growing use of roads and highways as the major mode of transportation, which provides flexibility. Other developments include new communications and refrigeration technologies. Not only do processors find the product to be of better quality if processed closer to the point of production, but the process can be less costly. The consumer benefits, society benefits, local labor benefits, and so do local firms. The same is true with other industries in the United States moving from the high cost and congested Midwest and Northeast regions to the Southern states.

The past 30 years have seen some major shifts in geographical importance by types of agriculture in the U.S.A.

Following World War II, the southeastern states found themselves with soils that were nutritionally depleted. Decades of soil-robbing crops such as cotton, corn, and tobacco had taken its toll. There were few if any legumes that would support cattle which would provide an abundance of animal fertilizer. Commercial fertilizers were not yet proven. Land ownership was reduced to small units following the civil war and large plantation cultivation was not extremely common.

The Midwest was beginning to feel the effects of industrial expansion westward from the technologically advanced northeast and eastern seaboard. Farm land began to increase in value because of suburban population growth, factory expansion, extension of the highway network, and airport development. Once-small, self-sufficient, diversified farms began to give way to larger, heavily equipped, capital-intensive production units. This was particularly true of grain farming. And cash crops such as chicken, dairy, vegetables soon became highly specialized endeavors. Chickens (broilers for meat and layers for eggs) moved from small barnyard flocks into environmentally controlled buildings. Mechanical, hydraulic, electronic, and pneumatic technology came out of defense industries to be used by
farm equipment manufacturers. New technology began to cascade onto traditional farming from two general sources—equipment suppliers and chemical suppliers. This was in addition to the traditional farm implement manufacturers. Of course, new capital was essential. It soon became clear that traditional agricultural financing sources would not be adequate on a timely basis. The innovative manufacturing firms, who foresaw that the markets for their products and services would open quickly would, therefore, of necessity, have to provide capital as well as equipment.

Thus, it was that, as these new rapidly developing innovations began to take place, the manufacturer had to sell his products on credit. No longer would the farmer buy one brooder, for example, to warm 100 baby chicks during the first six weeks of growth. Instead he would buy a whole new chicken house, environmentally controlled with ventilators, heaters, coolers, thermostats, automatic watering devices, mechanical feeders, and lights, all controlled electronically with time clocks and limit switches. The manure would be mechanically removed and the house completely steam cleaned with tractors, tank wagons, and air pressure systems and it would be chemically disinfected with whole new lines of sanitation materials. At the same time, new, fast-growing specially-bred varieties of birds (and, later, animals) would come into being. Feed rations for rapid growth would develop from a nutrition technology that to this day remains on the forefront of research and production results.

Thus, the farmer who previously had a flock of 100 chickens which would reproduce themselves soon would have a choice forced on him by the economics of technological change—get out of the chicken business and specialize in something else, or get into the chicken business on an economically feasible scale.

In the latter case the new chicken house would cost $20,000 in 1960. It would hold 20,000 birds from one day old until 20 weeks old. Technology over
time reduced this grow-out period to 9 weeks, and yielded 5 batches per year. The feed, medication, power, equipment, management, and labor would demand a cash flow that was very unfamiliar to local bankers and production credit associations which practiced short-term, cash-crop credit. Later on, as the broiler industry became widespread in Maine, Delaware, Maryland, and Virginia, Georgia, Alabama, Mississippi, North Carolina, Texas, and Arkansas, local financing sources began to compete to supply the farmers' needs, both in long term and short term. Until then, however, the capital and the technology came from Midwestern and Eastern manufacturers and banks. Within a relative short period of time, 1950-1970, a rather quiet, nostalgic, self-sufficient, American agriculture became a very turbulent, dynamic, tremendously changing agriculture. In the Northeast and central Midwest, the farm supporting a family either grew in land size or in the intensity of land use. Farms in the western mid-continent states expanded into large grain farms, others went into large-scale cattle, hog, or turkey operations. Farms in the far west shifted into intensified large-scale dairy, cattle, poultry, eggs, vegetable and fruit operations, among others. The whole South or sunbelt from Virginia through Texas has probably experienced the most change—some have said that today it comprises the bread basket of American agriculture. It has grown so much in this capacity that it is now a major exporting region, both into other states and overseas.

Georgia, for example, in about one decade (1955-1965) grew from virtually no commercial animal agriculture to be the nation's largest broiler-producing state, to rank very high in turkeys and eggs, and more recently to become significant in feeder cattle and hogs.

These shifts and changes took place in sequencing regional locations and in sequencing segments of agriculture following typical growth curves or life cycles. Thus, first came the poultry industry with new technologies for breeding, hatching, feeding, producing, slaughtering, processing, packaging,
distributing, and marketing of turkeys, broilers, fowl and eggs. Next the swine or hog industry developed, followed by cattle/calves. Concurrently, the legumes, grasses, grain and oil seeds were developing, as were citrus, vegetable, and fruits.

At the same time, a whole new industry developed called "agricultural chemicals." Many of the existing companies identified and separated operations into agricultural divisions. Monsanto, Allied Chemical, Pfizer, IMC, Swift, Armour were but a few of the prominent names. New companies were also born. The agricultural chemical business then became even more specialized as research and new needs emerged. Two types of chemicals then became separated--fine chemicals and heavy chemicals. These were primarily for the plant side of agriculture. Fine chemicals included: growth stimulants, insecticides, herbicides, etc; heavy chemicals included the fertilizer chemicals of nitrogen, phosphorous, and potash. The commercial fertilizer industry had begun. In addition, many of the above companies further specialized into chemicals for plant agriculture (above) and then into animal agriculture. The latter included growth stimulators, vaccines, health remedies, pesticides, and sanitation products.

While the above-named companies were large in their beginning into agriculture, much new growth would be injected because of their extensive research capability. Later on, some of these chemical and pharmaceutical firms would be able to use their agricultural research for human products. For example, cancer, typhoid, cold, vitamins, and blood research in chickens and animals lead to later breakthroughs for humans.

New companies sprung up all over the country to provide research, manufacturing, and services. Some of these succeeded, some failed, some were acquired by other firms as the industry expanded and grew.

The U.S. Department of Agriculture, The Food and Drug Administration,
and other government agencies also grew and improved their services during this era. They provided both facilitative functions and regulative functions.

Similar developments took place in equipment. Mechanization and automation became common vocabulary terms in both plant and animal agriculture. Farm implement manufacturers developed bigger tractors and auxiliary equipment. Short-line manufacturers specialized in pull-type equipment for planting, cultivating and harvesting. The barnyard equipment manufacturers developed products to reduce labor, standardize output and increase productivity in animal and poultry agriculture. Old-line companies such as John Deere, Allis Chalmers, Case Equipment brought in new technology.

Many new companies emerged when inventors and others developed new products in the typical small-business fashion. Later, as concentration and mergers took place, some of the major companies to evolve were outgrowths of firms which started in the Southeast. For example, as changes in product lines, in customer profiles, and in markets took place, firms would readjust by selling or buying single-product lines or firms. Over time, a whole new configuration of the agribusiness subsectors would emerge. Ownership would change and sources of technology would also change.

Major equipment innovators such as the Buckeye Corporation would grow, split, and become part of others. Thus, the Buckeye Incubator Company was founded in 1881. It manufactured metal supplies for feeding and watering poultry. In 1954, under new management (including the author), it began to expand in products, grow in sophistication of research, marketing and manufacturing, and spread in the geographic area served. Being homebased in Springfield, Ohio, with 2000 distributors, it converted to 22 factory sales branches, 10 of which were in the southeastern states by 1964. The company's changed name, had become publically owned and became a recognized leader in the mechanization and financing of animal agriculture. Vertical integration was occurring rapidly
so processing and packaging equipment were added. International expansion followed. Later the company was bought, product lines were sold off, and new directions were evident. This scenario happened to a large number of companies. Furthermore, in the 1960's, these firms were expanding to foreign countries; today a number of U.S. firms are owned by foreign firms.

3. CURRENT STATUS OF AGRIBUSINESS IN THE SOUTHEAST

The capital to accomplish all these dynamic changes during the 1950's and 60's came largely from sources outside the Southeast. Much capital came from outside typical agricultural finance.

In the 1970's this changed as the products, the firms, and the regional shifts matured. In fact, depending on one's view, it could be said that the life development curve may have "peaked out" for some commodities or some regions. For example, while Georgia had become the number one broiler-producing state in the 1960's, it lost out to Arkansas in the 1970's as that state showed lower costs and more labor availability.

Today very little shifting of commodities between regions is occurring, acquisitions or divestments by firms have diminished in number, and the remaining technological advancements seem to be in the area of logistics (in catching and crafting of birds, for example, to be shipped for processing). Capital is being infused largely in the region of use.

The vertical integration forward and backward seems to have slowed considerably. The large grain companies which provided animal feed and moved into production have since retreated in favor of private production. Large producers have integrated into feed manufacturing and product marketing. Some brand-image development has taken place. For example, in the commercial egg business it was recently estimated that 82 million layers are owned by 41 operators. A significant number of these are located in the Southeast.
These same general trends apply across all agriculture, and particularly in the Southeast. The trends in production and in marketing have been toward fewer and fewer firms or farms; larger and larger size; more specialization, sometimes into several areas (broilers and hogs, grain and cattle, vegetables and citrus); most organizations have sophisticated management practice, using computers for information processing and electronic communications for information transmittal (prices, supplies, forecasts). For example, the soybean harvest in Brazil, the wheat harvest in Russia, the tuna catch off Peru, or the strawberry harvest in Mexico are equally important to some agriculturalists as are the spot egg prices in Chicago, the cattle prices in Kansas City, or the tomato or citrus forecast from Florida to other producers and marketers.

4. SUMMARY

The decades of the 1950's, the 60's, and the 70's have witnessed dramatic and sometimes turbulent changes in American agribusiness. The changes in the Southeast have sometimes lead, sometimes followed, and sometimes paralleled other regional changes. The one-time small farmer who sold his output to, and through, a whole series of small businesses to reach the consumer is a rarity today.

As the subsectors of agriculture each experienced its life development cycle; as production and marketing functions in the distribution channels became compressed; as vertical and horizontal integration ebbed and flowed with new demands; as sophisticated management developed; as new capital and technology mushroomed into growth opportunities; and as ownership developed in large as well as small organizations, so has the term "agribusiness" gained full meaning—"from producer to consumer."

Today, American agriculture can be said to be "a very mature industry, made up of a composite of also very mature subsectors." For example, a very
large food and beverage company located in the Southeast has a computerized simulation model of the worldwide citrus industry. A large farmer cooperative, again based in the Southeast, imports and exports literally hundreds of agricultural products routinely. Standard operating practice on most farms today is to have fingertips access to market information. Many producers use the computer to arrive at ideal feed rations based on availability of costs or to determine best planting date based on climatic and soil condition data.

Today, American agribusiness is composed mostly of very well-managed organizations which have survived extremely competitive and yet often regulated times. The size of the firm and its areas of endeavor have been arrived at through trial, error, opportunity and good fortune. There are small business firms that are well established and fit a niche.

This author was a line officer in one of the leading manufacturing firms of the 1950's and 60's; and, as a consultant, has since conducted numerous planning and acquisition studies for large clients. It is his considered opinion that at this time there is very little opportunity for new entrants as small businesses in the traditional agribusiness framework. There may be opportunities for buy-outs of existing small business or changes of ownership in certain locales. But the opportunity for a man or woman to start a business and build it through volume, increase of market share, mergers and acquisitions, and public stock offerings, as many did previously, is very, very limited if existent at all.

A few opportunities for short-run exploitation may remain. For example, with the increasing amount of foreign capital coming into American agribusiness and farm land ownership, one might envision opportunities for consulting, brokerage, or management services. But as stated above, with agribusiness being very mature, with growth slowed or declining, with market shares established, and with capital and management well-positioned, the
situation is one of very limited opportunities for new entrants, particularly small businesses.

It is further complicated by the fact that so much of the technological advancements in agribusiness were based on cheap energy (fuel for tractors and trucks; electrical power for mechanized operations, and petrochemicals for fertilizers, etc.). This picture has changed dramatically with the escalating costs of energy. As this is being written, a morning newscast shows truckers striking and demonstrating because of the high cost of diesel fuel. Their professed rationale is that the consumer will feel it within one week in food supplies. What better example of how American agribusiness is closely tied to other segments of the economy today; and agribusiness in the Southeast has played and continues to play a very significant role.
REFERENCES


W. David Hopper, "The Development of Agriculture in Developing Nations,"
TAXATION OF SMALL BUSINESS IN REGION IV

K. Mark Weaver
The University of Alabama

1. SUMMARY

This study reports and analyzes the related concerns of small businesses. Data were collected via a mail survey to a total of 4998 small business persons in eight southeastern states. The respondents were biased upward in firm size, indicating that the larger firms may be more likely to respond to research of this type. In addition, the sample was selected from the membership roster of a major national association and some undetected bias could be introduced.

Some of the policy indicators derived from the analysis are:

1. People are dramatically upset and disturbed by the perceived inequity of the existing situation. For example, in the attitudinal statements in the survey, 95.1% of the firms expressed some level of agreement that "larger firms are better able to take advantage of tax regulations."

2. Concern with survival and with the ability to expand were examined in five statements. Insufficient tax incentives and policies which seem prohibitive are clearly felt to exist. For example, the most extreme position in the statements, that the "total tax burden on my firm could cause me to close my current business" still showed an agreement level of nearly 60%.

3. Concern with the complexity and "paperwork" aspects of taxes is represented by levels of agreement with three statements of 95%, 75.6% and 92.6%.

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4. Based on structure, 45% of the reporting firms indicated that payroll taxes were the most burdensome in terms of dollar cost.

5. For 1-4 and 50-99 employment categories, income taxes are the costliest; for all other sizes, payroll taxes are significantly more costly. Based on gross receipts, the very smallest (less $50,000) and largest ($3,000,000 and more) are the only categories for which income taxes exceed payroll taxes in cost.

6. Written comments to an open-ended question show that, of single changes in the tax system, the 3 most mentioned were to reduce payroll taxes, to reduce tax rates and simplify regulations and forms. Examples of written responses are included in the paper.

7. Proposals regarding changes reveal a general feeling that any of the changes would help. The comments related to suggested changes were overwhelming in the view that something must be done. The most even distribution of response was to the idea of "making tax regulations and laws apply on an equal basis regardless of business forms;" 35.1% of the people did not feel that this would help or had no opinion.

8. Despite the negative attitudes toward the tax system, as many as 29.5% of the respondents had no opinion about specific change. This "no opinion" response is highest in the smaller firms and could be related to availability of information.

9. In general, it appears that tax reductions and simplification issues are favored over credits and new, complex regulations.

10. An experimental attempt at discriminant analysis suggests that more "sophisticated" firms (i.e., firms with a CPA, more employees, and who pay to have tax work completed) were more positive toward credits than smaller, less sophisticated firms.

Tables presenting this information and discussion of the responses are
The comments and responses of small businesses show a strong concern with survival. What will happen to their firms? How can they pay the payroll taxes and still afford to expand? When will the number of forms, rules and regulations which require lawyers and accountants as a hidden cost of taxation ever change? Why are small firms seemingly ignored in most of the tax planning?

Specific changes in existing policy desired by small business firms include:

1. Stop using FICA taxes as a ruse for social welfare programs. Reduce the burden in terms of dollar cost and reporting.

2. Stop using lawyers to finalize tax regulation. Let someone who has to use them to stay out of jail and to keep a business operating review the regulations.

3. Think about the impact of the regulations on a firm. For example, the change from a general jobs credit to target credits severely limits the few firms apparently participating and using the job credits.

4. Require a "full tax" impact study. If a tax is passed that is reasonably expected to require outside assistance, calculate that cost in determining the total tax burden.

5. Provide industry-wide risk-adjusted long-term capital gains calculations to adjust for differences in the equity investments of smaller and larger firms. For example, if one type of firm has twice as high a risk, the capital gains tax could be reduced by more than one half to encourage development with equity instead of debt capital.

6. Allow reinvestment of profits (at some level, i.e. first $25,000) with deferred taxation to generate expansion capital.

7. Provide a "no-fault/no-risk" tax advisory service to small firms so they can determine whether or not they are complying with the law without
risking a penalty or jail term with no chance to correct the situation.

8. Simplify depreciation rules, recognizing the increased replacement costs and real effective life of assets.

9. Eliminate all inheritance taxes on business property which are passed to related parties for small firms. For example, a total asset limit was proposed by one respondent.

10. Make cash accounting legal for tax purposes so firms can have "one set of books." Differences in tax rules and common practice only confuse the firms and indications are that small firms pay a higher effective tax rate than larger firms.

In summary, while it is not scientific or based on any one statistical result, it seems that the respondents want a chance to succeed and some consideration of their needs when regulations are prepared.

2. INTRODUCTION

What Is A Small Business

One of the major difficulties confronting any analysis of the problems of small businesses is in the definition of a small business. Generally, the small business enterprise is categorized by factors such as follow here:

- few owners, most of whom are actively involved in the business
- most often organized as sole proprietorships, partnerships, or Subchapter S corporations
- localized area of operations
- relatively unsophisticated level of business systems
- orientation toward service or merchandising activities
- limited access to external financing
- limited amounts of capital.
The Impact of Small Businesses

The impact of small businesses on the American economy is anything but small. Small businesses represent 97% of the Nation's business entities and generate 43% of the Nation's national product (48% of the gross business product). Small businesses generate significantly over 50% of the Nation's total dollar volume generated by wholesaling, retailing, services provided, and construction. The major contribution of small businesses is not demonstrated by these statistics, however. By their very nature, small businesses constitute the major component in the theory and practice of free enterprise through their number, diversity, and geographic dispersion.

Taxation - The Impact on Small Business

The first major recognition given by Congress to the problems of small businesses was the enactment of certain provisions in the 1954 Tax Code. Recognizing that certain of these changes were not broad enough, the Senate instituted a major investigation of small business tax problems. Certain legislation was enacted in 1958 as a result of this investigation.

Little further attention was given to small business problems until early 1967, when the Senate began a continuing study of the tax system from the standpoint of small business. This research led to a comprehensive small business tax bill (the Bible-Evins bill), certain provisions of which have been enacted in some form in legislation subsequent to 1973.

The House and Senate Small Business Committee has held hearings on every tax proposal since 1973. Some provisions affecting small businesses have been enacted, partly through these hearings, but there have been no further comprehensive small business tax bills. The U.S. Small Business Administration, under P.L. 94-305 (Section 202[4]) has undertaken a study to determine the impact of taxation on small businesses and to propose legislative
and other changes.

This study specifically focuses on tax problems and related tax issues for small firms in the Southeast. Issues related to the import of current taxes on small firms are specifically addressed. Also, attitudinal positions of small business owners are reviewed as guides to programmatic and tax code revisions.

3. METHODOLOGY

Sampling Procedure

Data for this study were collected by a mail questionnaire sent to members of a national small business association in June 1979. The respondents were drawn from the total membership rolls of the association in the eight states in Federal Region IV. A sample of 4998 firms was chosen based on the following stratifications:

a. Ratio of number of firms in region to number of firms in each state determined how many firms would be surveyed in each state.

b. The distribution of firms by type of business (i.e., retail, service, etc.) was used to determine the number of firms by type.

c. The size distribution of firms in the state, by type of firms, was then used to finalize the sample.

All respondents were then randomly selected based on these three criteria.

The mailing was to 4998 firms with a cover letter from the president of the trade association. A second mailing of 4998, in the form of a reminder letter and a new questionnaire was sent approximately two weeks later.
The follow-up resulted in a total usable return of 1332 responses. The response rate of 26.7% is similar to other return rates for this population.

Sample Profile

The demographic profile of the respondents is presented in Table 1. A comparison of key response variables to the latest published data by the cooperating association shows that the respondents to the present study clearly parallel previous data. Thus by form of organization, the samples are quite close:

<table>
<thead>
<tr>
<th>Form</th>
<th>Prior Data</th>
<th>Current Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proprietorship</td>
<td>35%</td>
<td>37.1%</td>
</tr>
<tr>
<td>Partnership</td>
<td>9%</td>
<td>8.9%</td>
</tr>
<tr>
<td>Corporation</td>
<td>49%</td>
<td>46.1%</td>
</tr>
<tr>
<td>Subchapter S Corporation</td>
<td>7%</td>
<td>7.9%</td>
</tr>
</tbody>
</table>

Since size is a major consideration in this study, two size comparisons are shown below:

<table>
<thead>
<tr>
<th>Number of Employees</th>
<th>Prior</th>
<th>Current Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4</td>
<td>46%</td>
<td>47.3%</td>
</tr>
<tr>
<td>5-9</td>
<td>18%</td>
<td>21.5%</td>
</tr>
<tr>
<td>10-19</td>
<td>16%</td>
<td>15.7%</td>
</tr>
</tbody>
</table>

(Other employment sizes are not direct comparisons due to range differences.)

<table>
<thead>
<tr>
<th>Gross Receipts</th>
<th>Prior</th>
<th>Current Study</th>
</tr>
</thead>
<tbody>
<tr>
<td>Under $50,000</td>
<td>11.0%</td>
<td>12.2%</td>
</tr>
<tr>
<td>$50-100,000</td>
<td>20.3%</td>
<td>15.0%</td>
</tr>
<tr>
<td>$100-200,000</td>
<td>16.0%</td>
<td>16.6%</td>
</tr>
<tr>
<td>$3,000,000 and over</td>
<td>8.0%</td>
<td>6.1%</td>
</tr>
</tbody>
</table>

The similarity in these key profile characteristics is a strong
Table 1
DEMOGRAPHIC PROFILE OF THE RESPONDENTS

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Percentages</th>
<th>Number Responding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Form of Organization:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proprietorship</td>
<td>37.1</td>
<td>457</td>
</tr>
<tr>
<td>Partnership</td>
<td>8.9</td>
<td>110</td>
</tr>
<tr>
<td>Corporation</td>
<td>46.1</td>
<td>568</td>
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<tr>
<td>Subchapter S Corporation</td>
<td>7.9</td>
<td>98</td>
</tr>
<tr>
<td>Major Business Activity:</td>
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<td></td>
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<tr>
<td>Construction</td>
<td>8.9</td>
<td>121</td>
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<tr>
<td>Manufacturing</td>
<td>1.1</td>
<td>15</td>
</tr>
<tr>
<td>Transportation</td>
<td>11.4</td>
<td>155</td>
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<tr>
<td>Wholesale</td>
<td>6.0</td>
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<tr>
<td>Retail</td>
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<tr>
<td>Agriculture</td>
<td>10.9</td>
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<tr>
<td>Financial</td>
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</tr>
<tr>
<td>Service</td>
<td>31.0</td>
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<td>Professional</td>
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<tr>
<td>Number of Employees:</td>
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<tr>
<td>1-4</td>
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<tr>
<td>5-9</td>
<td>21.5</td>
<td>290</td>
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<tr>
<td>10-19</td>
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<td>211</td>
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<tr>
<td>20-49</td>
<td>11.3</td>
<td>152</td>
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<tr>
<td>$0-99</td>
<td>2.8</td>
<td>33</td>
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<tr>
<td>100+</td>
<td>1.4</td>
<td>19</td>
</tr>
<tr>
<td>Years in Business:</td>
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</tr>
<tr>
<td>1-5</td>
<td>25.7</td>
<td>344</td>
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<tr>
<td>6-10</td>
<td>19.7</td>
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<tr>
<td>11-15</td>
<td>14.1</td>
<td>188</td>
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<tr>
<td>16-20</td>
<td>11.8</td>
<td>157</td>
</tr>
<tr>
<td>Greater than 20</td>
<td>27.9</td>
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</tr>
<tr>
<td>Gross Receipts during latest calendar year:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Under $50</td>
<td>12.2</td>
<td>163</td>
</tr>
<tr>
<td>$50-$100</td>
<td>20.3</td>
<td>271</td>
</tr>
<tr>
<td>$100-$200</td>
<td>16.6</td>
<td>222</td>
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<tr>
<td>$200-$350</td>
<td>14.1</td>
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<tr>
<td>$350-$500</td>
<td>7.9</td>
<td>106</td>
</tr>
<tr>
<td>$500-$750</td>
<td>6.7</td>
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<tr>
<td>$750-$1000</td>
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<td>79</td>
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<tr>
<td>$1000-$5000</td>
<td>10.2</td>
<td>137</td>
</tr>
<tr>
<td>$5000 and over</td>
<td>6.1</td>
<td>82</td>
</tr>
<tr>
<td>Franchise:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yes</td>
<td>9.1</td>
<td>122</td>
</tr>
<tr>
<td>No</td>
<td>90.9</td>
<td>1215</td>
</tr>
<tr>
<td>State Business is located:</td>
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<td></td>
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<tr>
<td>Alabama</td>
<td>8.6</td>
<td>117</td>
</tr>
<tr>
<td>Mississippi</td>
<td>4.8</td>
<td>65</td>
</tr>
<tr>
<td>Georgia</td>
<td>15.5</td>
<td>211</td>
</tr>
<tr>
<td>Florida</td>
<td>30.5</td>
<td>414</td>
</tr>
<tr>
<td>North Carolina</td>
<td>13.1</td>
<td>178</td>
</tr>
<tr>
<td>South Carolina</td>
<td>6.3</td>
<td>85</td>
</tr>
<tr>
<td>Tennessee</td>
<td>10.2</td>
<td>159</td>
</tr>
<tr>
<td>Kentucky</td>
<td>11.0</td>
<td>149</td>
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</tbody>
</table>
Table 1 (continued)
DEMOGRAPHIC PROFILE OF THE RESPONDENTS

<table>
<thead>
<tr>
<th>Characteristic</th>
<th>Percentages</th>
<th>Number Responding</th>
</tr>
</thead>
<tbody>
<tr>
<td>Maintenance of Accounting Records:</td>
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<td></td>
</tr>
<tr>
<td>Owner</td>
<td>26.3</td>
<td>353</td>
</tr>
<tr>
<td>Firm's Bookkeeper</td>
<td>20.5</td>
<td>276</td>
</tr>
<tr>
<td>Accountant other than C.P.A.</td>
<td>15.3</td>
<td>206</td>
</tr>
<tr>
<td>C.P.A.</td>
<td>37.3</td>
<td>501</td>
</tr>
<tr>
<td>Other</td>
<td>.6</td>
<td>8</td>
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<tr>
<td>Preparation of Business tax returns:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal Income Tax</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Owner</td>
<td>10.4</td>
<td>139</td>
</tr>
<tr>
<td>Firm's Bookkeeper</td>
<td>6.5</td>
<td>87</td>
</tr>
<tr>
<td>Accountant-Non C.P.A.</td>
<td>20.6</td>
<td>276</td>
</tr>
<tr>
<td>C.P.A.</td>
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<td>812</td>
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<td></td>
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<tr>
<td>Owner</td>
<td>29.9</td>
<td>359</td>
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<tr>
<td>Firm's Bookkeeper</td>
<td>29.4</td>
<td>353</td>
</tr>
<tr>
<td>Accountant-Non C.P.A.</td>
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</tr>
<tr>
<td>C.P.A.</td>
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<td>309</td>
</tr>
<tr>
<td>Other</td>
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<td>17</td>
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<tr>
<td>F.I.C.A.</td>
<td></td>
<td></td>
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<tr>
<td>Owner</td>
<td>24.1</td>
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</tr>
<tr>
<td>Firm's Bookkeeper</td>
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</tr>
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</tr>
<tr>
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<td>329</td>
</tr>
<tr>
<td>Other</td>
<td>1.4</td>
<td>17</td>
</tr>
<tr>
<td>Unemployment Tax</td>
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<td></td>
</tr>
<tr>
<td>Owner</td>
<td>23.5</td>
<td>294</td>
</tr>
<tr>
<td>Firm's Bookkeeper</td>
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<td>421</td>
</tr>
<tr>
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<tr>
<td>C.P.A.</td>
<td>26.3</td>
<td>332</td>
</tr>
<tr>
<td>Other</td>
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<tr>
<td>Other Taxes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Owner</td>
<td>22.9</td>
<td>287</td>
</tr>
<tr>
<td>Firm's Bookkeeper</td>
<td>24.8</td>
<td>311</td>
</tr>
<tr>
<td>Accountant-Non C.P.A.</td>
<td>15.9</td>
<td>199</td>
</tr>
<tr>
<td>C.P.A.</td>
<td>35.0</td>
<td>438</td>
</tr>
<tr>
<td>Other</td>
<td>1.4</td>
<td>17</td>
</tr>
<tr>
<td>Use of outside Accounting Services:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Yes</td>
<td>28.7</td>
<td>365</td>
</tr>
<tr>
<td>No</td>
<td>58.7</td>
<td>745</td>
</tr>
<tr>
<td>Not applicable</td>
<td>12.6</td>
<td>160</td>
</tr>
<tr>
<td>Cost of Tax Returns:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Under $500</td>
<td>35.3</td>
<td>466</td>
</tr>
<tr>
<td>$501-$1000</td>
<td>27.7</td>
<td>366</td>
</tr>
<tr>
<td>$1001-$1500</td>
<td>11.8</td>
<td>155</td>
</tr>
<tr>
<td>$1501-$2500</td>
<td>9.2</td>
<td>121</td>
</tr>
<tr>
<td>Greater than $2500</td>
<td>10.3</td>
<td>130</td>
</tr>
<tr>
<td>Not applicable</td>
<td>5.7</td>
<td>75</td>
</tr>
<tr>
<td>Costliest tax:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Payroll taxes</td>
<td>44.8</td>
<td>597</td>
</tr>
<tr>
<td>Income or Corporate income tax</td>
<td>36.8</td>
<td>490</td>
</tr>
<tr>
<td>Property and/or inventory tax</td>
<td>7.4</td>
<td>98</td>
</tr>
<tr>
<td>Other</td>
<td>1.1</td>
<td>14</td>
</tr>
<tr>
<td>Uncertain</td>
<td>10.0</td>
<td>133</td>
</tr>
<tr>
<td>Tax most need of reform:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Social Security tax (FICA)</td>
<td>51.8</td>
<td>689</td>
</tr>
<tr>
<td>Unemployment Compensation tax</td>
<td>14.4</td>
<td>192</td>
</tr>
<tr>
<td>Sales or excise tax</td>
<td>1.7</td>
<td>22</td>
</tr>
<tr>
<td>Property tax</td>
<td>2.9</td>
<td>38</td>
</tr>
<tr>
<td>Business Income tax</td>
<td>16.0</td>
<td>213</td>
</tr>
<tr>
<td>Other</td>
<td>6.6</td>
<td>8</td>
</tr>
<tr>
<td>Undecided</td>
<td>12.6</td>
<td>167</td>
</tr>
</tbody>
</table>
indication that the data can be compared with other data.

The tax-related information contained in the profiles was not directly comparable to other sources but does show some highly visible results for tax planning and policy formulation.

The accounting records are maintained by a non-CPA in over 62% of the firms. Even federal taxes are prepared by someone other than a CPA in 37.5% of the firms. The combination of these factors should be a clear message to policy makers. In small firms doing their own record keeping, relevant tax data, documentation and information will be lacking. Based on consulting experiences, the author would contend that the poorly maintained records will result in tax problems. It should be no surprise that simplicity and reduction of paperwork is such a pressing issue.

The profiles show that tax preparation is neglected through a failure to use trained personnel and in the low cost of tax preparation.

In terms of cost and need for reform, payroll taxes are clearly the greatest concern of small business firms. Additional discussion of respondent comments appears in the statement analysis section.

The profiles offer a chance to review the sources of the responses discussed in the following sections. The similarity to prior research provides a positive base for this analysis.

4. ANALYSIS AND DISCUSSION OF ATTITUINAL RESPONSES

The purpose of this section is to report the responses to the tax-concern statements and to indicate why such strong sentiments may be expressed. Table 2 shows the distribution of responses to the tax concerns. Items 3, 10, and 11 are primarily concerned with survival and expansion issues. The complexity issues seen in Items 1, 5 and 8 are intertwined with these two issues. The following sections address all three areas of concern and
## TABLE 2
ATTITUINAL RESPONSES TO TAX CONCERNS

**PART II**

Listed below are 11 statements addressing tax concerns in small business. Please indicate your level of agreement for each statement.

<table>
<thead>
<tr>
<th>Statement</th>
<th>Strongly Agree</th>
<th>Agree</th>
<th>Slightly Agree</th>
<th>Slightly Disagree</th>
<th>Disagree</th>
<th>Strongly Disagree</th>
<th>No Opinion Or Does Not Apply</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. The necessary paperwork required to comply with federal tax regulations and filing requirements is too complex for small business.</td>
<td>792 58.8</td>
<td>390 29.0</td>
<td>97 7.2</td>
<td>22 1.6</td>
<td>22 1.6</td>
<td>4 0.3</td>
<td>19 1.4</td>
</tr>
<tr>
<td>2. There are insufficient tax incentives to provide needed capital for small business start-ups and expansions.</td>
<td>675 50.6</td>
<td>428 32.1</td>
<td>68 5.1</td>
<td>15 1.1</td>
<td>47 3.5</td>
<td>23 1.7</td>
<td>77 5.8</td>
</tr>
<tr>
<td>3. A national sales tax would be more fair than a tax on profits.</td>
<td>337 26.1</td>
<td>287 22.2</td>
<td>119 9.2</td>
<td>44 3.4</td>
<td>198 15.3</td>
<td>79 6.1</td>
<td>228 17.6</td>
</tr>
<tr>
<td>4. Current taxes on business profits are prohibitive to small business expansions.</td>
<td>577 43.4</td>
<td>486 36.5</td>
<td>136 10.2</td>
<td>32 2.4</td>
<td>30 2.3</td>
<td>5 0.4</td>
<td>64 4.8</td>
</tr>
<tr>
<td>5. Federal tax advisory and assistance programs do not give enough help to small business.</td>
<td>475 35.9</td>
<td>429 32.4</td>
<td>136 10.3</td>
<td>26 2.0</td>
<td>35 2.6</td>
<td>12 0.9</td>
<td>211 15.9</td>
</tr>
<tr>
<td>6. The increase in taxes based on payroll (FICA) is a major hindrance to expanding employment.</td>
<td>706 52.8</td>
<td>358 26.8</td>
<td>126 9.4</td>
<td>33 2.5</td>
<td>49 3.7</td>
<td>5 0.4</td>
<td>59 4.4</td>
</tr>
<tr>
<td>7. The total tax burden on my firm could cause me to close my current business.</td>
<td>241 18.2</td>
<td>250 18.9</td>
<td>290 21.9</td>
<td>114 8.6</td>
<td>273 20.6</td>
<td>50 3.8</td>
<td>107 8.1</td>
</tr>
<tr>
<td>8. Compliance with tax regulation requires outside professional service (i.e., accountant, lawyers, etc.).</td>
<td>785 58.5</td>
<td>396 29.5</td>
<td>62 4.6</td>
<td>17 1.3</td>
<td>29 2.2</td>
<td>6 0.4</td>
<td>46 3.4</td>
</tr>
<tr>
<td>9. Current tax incentives (i.e., job credit, investment credit, etc.) are useful in my firm.</td>
<td>233 17.7</td>
<td>279 21.1</td>
<td>214 16.2</td>
<td>63 4.8</td>
<td>240 18.2</td>
<td>95 7.2</td>
<td>196 14.8</td>
</tr>
<tr>
<td>10. Large firms can better take advantage of complex tax regulations than can small firms.</td>
<td>858 64.1</td>
<td>382 28.5</td>
<td>33 2.5</td>
<td>6 0.4</td>
<td>16 1.2</td>
<td>6 0.4</td>
<td>38 2.8</td>
</tr>
<tr>
<td>11. Tax rate reductions are more helpful than increases in the investment tax credit.</td>
<td>615 46.15</td>
<td>441 33.3</td>
<td>75 5.7</td>
<td>16 1.2</td>
<td>25 1.9</td>
<td>11 0.8</td>
<td>141 10.6</td>
</tr>
</tbody>
</table>
attempt to show how the "big business" bias (sensed in Item 10) is related to sources of financing and to show the difficulty in complying with regulations even where incentives are provided.

In the final section, response to the proposed tax changes are summarized in Table 4. The response to the proposed changes will be reviewed based on discussions of the key tax-concern areas and policy implications.

The survival of any business, small or large, depends heavily on its ability to generate sufficient capital. The retention of competent employees, the acquisition of materials and equipment, and the development of markets for products and services depend on the existence of adequate capital. In inflationary periods, labor costs and the costs of replacing inventories and equipment increase at such a pace that an enterprise must continually increase its capital base merely to hold its position. Businesses depend on four traditional sources from which to obtain capital: new equity, borrowing, retained earnings, and capital recovery systems (depreciation and the investment tax credit). Our system of taxation has very definite effects on each of these sources of capital.

New Equity Capital

Solomon Brothers calculated that in 1978, the equity markets would supply only 8.7% of the cash needed by U.S. businesses, as compared with 10% in 1977. That 8.7% was the smallest amount of capital provided by the equity markets for any year since 1974. Mutual funds, pension funds, and bank trust departments now represent a significant portion of the equity markets. These entities tend to favor (or are required by law to invest in) "blue-chip" investments. Additionally, a significant portion of the funds which could be available for investment are controlled by large corporations that first fulfill their needs for capital before distributing the remaining
funds to their shareholders. Given these points, it is easy to see that equity capital available for investment in small business is likely to be scarce, and the sources of such equity capital are likely to consist to a large degree (at least) of individual investors. Our system of taxation acts to effectively channel the equity capital of individual investors away from small businesses.

Tax policy tends to depress incentives or (at least) channel equity capital into particular areas, often at the expense of small businesses. Given long-term capital gains (see below), accelerated depreciation methods, oil depletion, and other such programs, tax breaks attract risk money into specific types of capital-intensive investments such as land speculation, real estate (apartments, etc.), and oil exploration, and away from most other types of small businesses. The high concern with payroll taxes as seen in Item 6, strongly reinforces our view.

The taxation of long-term capital gains is considered to channel equity capital away from small businesses. While capital gains resulting from the sale or exchange of an equity interest in all businesses are taxed in a similar manner, the risks inherent in small business ventures are, as a rule, significantly greater than for large businesses. Given the same tax treatment on the ultimate disposition of an investment, a potential investor will obviously choose the least risky among investment alternatives, thus discouraging investors from committing their investment funds to the small business sector. This area corresponds to the needs expressed in Items 4 and is an area where small firms obviously see room for change.

Tax policy also is by its nature biased against the retention of capital by small businesses. The bases for this inequity are discussed in the section below concerning earnings retention by small businesses. This bias against the retention of earnings prevents an adequate return to
stockholders in many cases, especially where funds are needed for capital investment and working capital. If an adequate return cannot be received by investors from a particular investment, that investment obviously will not receive the capital that it requires. An additional complication facing the generation of new equity capital is that our taxing system favors debt financing as opposed to equity financing.

**Borrowing**

Capital available for use as long-term investment capital most often is provided in the form of debt, at least partially due to the tax benefits extended to debt financing. By allowing the deduction of interest payments from gross income when determining taxable income for a particular year, the Internal Revenue Code reduces the cost of utilizing debt by a factor equal to the tax rate of the firm. This utilization of debt instead of equity can create difficulties for a small business.

If such funds can be borrowed at all, the riskier small business venture will probably have to pay a higher price for those borrowed funds. The use of debt as a primary capital source may cause a dangerously high debt-equity ratio which could decrease the chances of the survival of the small business during economically slow periods by hindering the establishment of an adequate equity base. The business' chances of survival during such periods of economic reverses also may be hindered by high fixed costs resulting from the large interest payments. Thus, the tax policy favoring debt over equity as a source of capital may provide an additional impetus to the failure of small businesses.

In addition to the problems caused by the excessive use of debt financing, tax policy creates additional problems with regard to the availability of debt capital by channeling loanable funds away from the small businesses
which desperately require those funds. Investors who can accept high-risk investments such as are provided by small businesses tend to have high incomes. These high tax-bracket investors are attracted to investments with the potential for the sheltering of income from taxation. The investor who seeks a fixed return (if he is not drawn to high-yield government securities) may be induced by tax considerations to invest in municipal securities, the income of which are tax-exempt. Thus, our system of taxation can serve to attract potential risk capital into highly conservative investments and away from small businesses.

Capital Recovery Systems

Capital recovery systems (depreciation and the investment tax credit, or ITC) are designed to allow taxpayers to recover the cost of property used in a trade or business, or of property held for the production of income. The ITC is designed to provide a stimulus to capital investment and it is available to all firms. However, most small firms are labor- rather than capital-intensive (as seen in the concern with payroll taxes). These firms do not have the investment in qualifiable assets which would allow the ITC to be of significant benefit. "Internal Revenue statistics for 1972 show that over 70% of the dollars recovered through ITC went to less than two-tenths of one percent of the corporations in the United States. And this concentration has accelerated in recent years."

Those small businesses that are sufficiently capital-intensive to be in a position to take significant advantage of capital recovery systems under the tax law are faced with a complex array of provisions: additional first-year depreciation, the ITC, ADR, accelerated depreciation and amortization methods, salvage value, disputes about useful lives, and recapture provisions. Smaller businesses do not have the resources to afford the battery of accountants, lawyers, and tax consultants used by their competitors, and so these small businesses rarely take advantage of so many advantageous capital
recovery methods. ADR (Asset Depreciation Range) is a good example. Its application is very complex and most smaller businesses avoid it religiously. Only 2% of businesses with assets between $500,000 and $1 million use ADR while 63% of those firms with assets over $1 billion use it. Items 5, 8 and 10 in Table 2 are indicative of individual concerns with these areas.

Retained Earnings

As can be inferred from earlier discussions, small businesses are quite often forced to finance themselves largely through the reinvestment of their own earnings due to the inaccessability of traditional outside sources of financing. Reinvested earnings are used to finance current operations and expansion as well as to cope with problems generated by inflationary pressures as well as economic slowdowns. The tax system is biased against the retention of earnings by small businesses.

The bias against the retention of earnings by small businesses is exhibited in the fact that small businesses often have higher effective rates of taxation than large businesses. Unincorporated businesses often pay at rates in excess of the statutory corporate rates due to steeply graduated individual rates. The significance of this fact can be illustrated by considering that, in 1974, 86.8% of all businesses, were proprietorships or partnerships, whose owners paid income taxes at those steeply graduated individual rates. Small corporations also may not be able to take advantage of certain tax incentives available to larger corporations, resulting in an often higher effective tax rate for the smaller corporations.

Our taxing system is designed in principle to tax those who have a greater ability to pay at higher rates. However, in practice, the taxing system has in the past consistently taxed smaller businesses at higher effective rates than larger businesses. Although the statutory corporate
tax rate is 48%, one out of every five big companies pays less than 43% and the largest 100 companies consistently pay between 25% and 30%. In contrast, medium-sized companies which are trying to expand into effective competitors must often pay the full statutory 48%, and sometimes even more than half their income in taxes" (Office of Advocacy, p. 409). Although the lowering of corporate tax rates in the Revenue Act of 1978 will help to lower the effective tax rate of smaller corporations, the basic causes of the inequities alluded to above still exist.

While tax incentives are available to all businesses through the Code, in reality these incentives are biased in favor of larger businesses. The benefits available under the Code most often pertain to the types of activities and levels of income encountered most often only to these larger businesses. The investment tax credit (ITC), foreign tax credit (FTC), and Domestic International Sales Corporation (DISC) provisions are prime examples. As mentioned in the preceding section, most small businesses are not of a type (capital intensive) which would allow them to benefit greatly from the ITC. The same is true of the FTC and DISC provisions.

The benefits of tax incentives related to export activities also are concentrated in larger businesses. As only 4% of the American business community and 12,000 out of 300,000 small manufacturers are engaged in international trade, most benefits of DISC and FTC provisions go to large, multinational firms. To further illustrate this concentration, also consider that firms with assets in excess of $250,000,000 receive 97% of the total FTC.

Payroll Taxes

The problems associated with payroll taxes (the payment thereof, and the related paperwork) are related both to small business problems
pertaining to the retention of earnings and the bias against small business resulting from the complexity of the tax system. However, this area is of such importance to small businessmen that a separate discussion of payroll tax problems is in order. The importance of payroll taxes can be seen in the response to Item 6 relating payroll taxes to limits on expansion and to the profile data in Table 1. Table 3 compresses the taxes to payroll, income and other tax related deductions.

Table 3

<table>
<thead>
<tr>
<th>Form of Business</th>
<th>Payroll</th>
<th>Type of Tax</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Proprietorship</td>
<td>33.7%</td>
<td>44.3%</td>
<td>22%</td>
</tr>
<tr>
<td>Partnership</td>
<td>44.5%</td>
<td>35.5%</td>
<td>20%</td>
</tr>
<tr>
<td>Corporation</td>
<td>54.3%</td>
<td>30.8%</td>
<td>14.9%</td>
</tr>
<tr>
<td>Subchapter S Corporation</td>
<td>44.3%</td>
<td>37.1%</td>
<td>18.5%</td>
</tr>
</tbody>
</table>

Annual Gross Receipts (1,000s)

<table>
<thead>
<tr>
<th></th>
<th>Payroll</th>
<th>Income</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than $50</td>
<td>25.6%</td>
<td>45.5%</td>
<td>28.8%</td>
</tr>
<tr>
<td>$50 - 100</td>
<td>42.0%</td>
<td>37.2%</td>
<td>20.8%</td>
</tr>
<tr>
<td>$100 - 200</td>
<td>45.6%</td>
<td>34.4%</td>
<td>20.0%</td>
</tr>
<tr>
<td>$200 - 350</td>
<td>55.4%</td>
<td>28.0%</td>
<td>16.7%</td>
</tr>
<tr>
<td>$350 - 500</td>
<td>55.8%</td>
<td>32.7%</td>
<td>11.5%</td>
</tr>
<tr>
<td>$500 - 750</td>
<td>53.3%</td>
<td>37.8%</td>
<td>8.8%</td>
</tr>
<tr>
<td>$750 - 1,000</td>
<td>55.8%</td>
<td>28.6%</td>
<td>15.6%</td>
</tr>
<tr>
<td>$1,000 - 3,000</td>
<td>45.1%</td>
<td>39.1%</td>
<td>15.8%</td>
</tr>
<tr>
<td>$3,000 and above</td>
<td>33.3%</td>
<td>53.1%</td>
<td>13.6%</td>
</tr>
</tbody>
</table>

Number of Employees

<table>
<thead>
<tr>
<th></th>
<th>Payroll</th>
<th>Income</th>
<th>Other</th>
</tr>
</thead>
<tbody>
<tr>
<td>1-4</td>
<td>34.7%</td>
<td>40.6%</td>
<td>24.8%</td>
</tr>
<tr>
<td>5-9</td>
<td>52.7%</td>
<td>34.3%</td>
<td>13.1%</td>
</tr>
<tr>
<td>10-19</td>
<td>56.5%</td>
<td>32.4%</td>
<td>11.2%</td>
</tr>
<tr>
<td>20-49</td>
<td>57.4%</td>
<td>31.8%</td>
<td>10.9%</td>
</tr>
<tr>
<td>50-99</td>
<td>39.4%</td>
<td>42.1%</td>
<td>18.4%</td>
</tr>
<tr>
<td>100+</td>
<td>66.7%</td>
<td>16.7%</td>
<td>16.7%</td>
</tr>
</tbody>
</table>

"In our company, in 1982, we will be paying more in social security taxes than we earned... and at that point, I am ready to give up. I think it is asinine... [The proportionally greater impact on small businesses can be illustrated by the fact that] I get $60,000 a year sales per employee
and somebody like General Motors gets $285,000" (U.S. Senate Committee on
Small Business, p. 63).

The problems surrounding payroll taxes (FICA and unemployment taxes) are in three major areas: paying the taxes, complying with the paperwork requirements, and the determination of employee status for payroll tax purposes.

Small Businesses with liquidity problems may find their cash flow problems compounded through the periodic deposits required for FICA and unemployment taxes. Additionally, the employer's share of FICA and unemployment taxes are levied on a base of wages per employee. If the employee leaves, the base amount (and therefore, the tax) begins again for the replacement employee. Thus, turnover can result in a multiple tax liability for the employer. Such a multiple tax liability can be especially severe for small firms with fewer financial resources.

Payroll tax reports are usually required by the various state, local, and federal taxing authorities at frequent intervals. Although most of these payroll tax reports contain substantially similar information, separate reports must be filed with the various taxing authorities. Small business persons perceive this as a useless duplication of effort.

A third major payroll tax problem concerns the determination of employee status for payroll tax purposes. No payroll tax withholding is necessary and no employer payroll taxes are payable if the person in question is considered to be a self-employed independent contractor. The classification as an employee or as a self-employed independent contractor is made based generally under the common law test of control. Subjective considerations involved in such determinations consume a great deal of time, both for the small businessman and the IRS. As small businesses are more labor intensive, this problem is more acute in this area. Barbers, contractors, real estate
brokers, and independent truckers (all falling within normal small business categories) have been hard hit by this problem.

Complexity of the Tax System - The Bias Against Small Business

The complexity of existing tax laws and regulations costs smaller businesses proportionally more than larger businesses. This cost can be attributed to the following instances. First, small businesses cannot afford the staffs of experts (remember payroll taxes!) necessary to recognize and deal with tax problems and to comply with all of the various aspects of state, local, and federal tax laws and regulations. Items 1, 5 and 8 in Table 2 are clear evidence of individual concern with these factors. The management personnel of small businesses must confront many varied types of problems in addition to those in the area of taxation. Management time spent on taxation matters takes proportionally more time and cost away from other, more profitable and productive activities in small business as compared to larger businesses.

Another case of proportionally higher cost to smaller business arises when outside expert advice cannot be retained in all areas in which such advice is needed. The costs of additional unnecessary taxes and penalties paid due to a lack of tax sophistication on the part of the small business surely are proportionally greater for those smaller businesses. The concerns expressed in response to parts II and III of the questionnaire clearly show this to be true. When the burden of the complexity of the tax laws is considered in terms of the additional costs it imposes on small business, it appears that smaller businesses may be placed in a position of a considerable competitive disadvantage.

The Proliferation of Paperwork

The multiplicity of different laws, regulations, procedures, and
forms which face the small businessman has become a heavy burden in terms of
cost and productivity loss. The federal, state, and local governments require
many types of reporting. The best way to illustrate this is to review some
of the requirements which face practically every small business. Remember,
this discussion is by no means all-inclusive (Based on the State of Alabama
system).

ON BEGINNING BUSINESS--The business must obtain from the local government
the appropriate business licenses and permits allowing it to operate.
Form SS-4 must be filed with the IRS as an application for a federal employer
I.D. number. The business must apply for a state sales tax license.
PERIODICALLY--The following listing represents some of the commonly
required filings facing most small businesses on at least an annual basis:

<table>
<thead>
<tr>
<th>Description</th>
<th>Form No.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal - Statement of employee taxes withheld</td>
<td>W-2</td>
</tr>
<tr>
<td>- Transmittal of income and tax statements</td>
<td>W-3</td>
</tr>
<tr>
<td>- Employer's annual FUTA return</td>
<td>940</td>
</tr>
<tr>
<td>- Employer's quarterly federal tax return for federal</td>
<td>941</td>
</tr>
<tr>
<td>income tax withheld from wages and FICA taxes</td>
<td></td>
</tr>
<tr>
<td>- Corporation income tax return</td>
<td>1120</td>
</tr>
<tr>
<td>- Corporation application for tentative refund</td>
<td>1139</td>
</tr>
<tr>
<td>- Corporation application for quick refund</td>
<td>4466</td>
</tr>
<tr>
<td>- Application for extension of time</td>
<td>7004</td>
</tr>
<tr>
<td>- Fiscal year corporation estimated tax</td>
<td>1120-W</td>
</tr>
<tr>
<td>- Computation of investment tax credit</td>
<td>3468</td>
</tr>
<tr>
<td>- Schedule of gains and losses on sales or exchanges of property</td>
<td>1120-D</td>
</tr>
<tr>
<td>- Depreciation schedule</td>
<td>4562</td>
</tr>
<tr>
<td>- Supplementary schedule of gains &amp; losses</td>
<td>4797</td>
</tr>
<tr>
<td>- New jobs credit</td>
<td>5884</td>
</tr>
<tr>
<td>State - Domestic corporation franchise tax return and</td>
<td></td>
</tr>
<tr>
<td>permit application</td>
<td>PT-2-1</td>
</tr>
<tr>
<td>- Domestic corporation income tax return</td>
<td>20</td>
</tr>
<tr>
<td>- Application for extension of time to file</td>
<td>20-E</td>
</tr>
<tr>
<td>- Application for refund of overpayment of estimated tax</td>
<td>ITRE-2</td>
</tr>
<tr>
<td>- Report of receipts - sales tax</td>
<td>ALT.</td>
</tr>
<tr>
<td>- Sales tax return</td>
<td>ST-1</td>
</tr>
<tr>
<td>- Schedule of locations, gross sales and collections,</td>
<td>ST-2</td>
</tr>
<tr>
<td>deductions and amount used as measure for tax</td>
<td></td>
</tr>
<tr>
<td>- Sellers Use Tax return</td>
<td>UT-4</td>
</tr>
</tbody>
</table>
Description | Form No.
--- | ---
State - Information for registration (use tax) | ----
cont'd. - Certificate of registration (use tax) | ----
- Employer's quarterly return of income tax withheld | A-1
- Employer's contribution and wage report | UC CR-4
City - Local city payroll tax quarterly return | ----

In addition to the forms above, employers must maintain on file up-to-date federal (Form W-4) and state (Form A-4) Employee's Withholding Allowance (Exemption) Certificates. Both federal and state governments impose penalties for late and/or incorrect filings of the various forms required. The proliferation of federal, state, and local paperwork staring every small businessman in the fact is truly staggering. Few educational opportunities exist which allow the small businessman to familiarize himself with even the broad opportunities and problems generated by the taxing system. As mentioned earlier, the results of such a lack of tax sophistication include additional costs to acquire outside professional assistance and additional taxes and/or penalties stemming from the missing of opportunities or failure to comply with all provisions of the law.

Retirement Benefits

The deductible amount a self-employed individual who is an owner-employee may contribute to a retirement profit-sharing plan for himself is limited to the lesser of $7,500 or 15% of his earned income during a taxable year. An owner-employee is a proprietor or, in the case of a partnership, a partner who owns either more than 10% of the capital interest, or more than 10% of the profit interest of the partnership.

Corporate retirement plan contributions for employees are subject to more lenient limitations. Where the plan embraces only a retirement trust,
the corporation may deduct either:

1. contributions in an amount actually necessary to pay the normal cost of the plan and amortize past service costs in equal annual payments (including interest and principal), or,

2. the amount necessary to provide the remaining unfunded past and current service credits of each employer, as a level amount or level percentage of compensation, over his remaining future service.

If the corporate plan embraces features of both a retirement plan and a profit-sharing plan, the limitation is the greater of 25% of the compensation paid to the employees covered by the plan or the amount necessary to satisfy the minimum funding standards set by I.R.C. Sec. 412. As can be seen from the above discussion, the corporate form generates much greater pension and profit-sharing plan deductions than does a non-corporate form. The unincorporated small businessman is thus faced with a significant disadvantage in this area.

Many types of fringe benefits may be provided for employees. Such benefits include group term life insurance, health insurance, disability insurance, death benefits, medical reimbursement plans, deferred compensation arrangements, and others. The corporation may deduct the cost of these benefits while the employees are not required to include the cost of such benefits in their income. Unincorporated businesses may not utilize the cost of such benefits as a deduction from taxable income.

4. ANALYSIS AND DISCUSSION OF PROPOSED CHANGES TO CURRENT TAX LAW

The major concerns and inequities in the tax law and regulations
as perceived by small business persons lead to a discussion of specific proposals. A recent NFIB Mandate specifically addressed two areas discussed previously and one directly related to Item 8 in Table 4. The items which dealt with reinvestment incentive proposed deferring income taxes on the first $25,000 in profits used for reinvestment (75% favored) and deferring capital gains taxes on the sale of a business in the proceeds which are reinvested in another small business within 18 months (70% favored). The items are similar in intent and scope to the accumulation of earnings in Item 10 and the inheritance tax provision in Item 7. These types of changes are direct, provide specific relief to foster growth in the small business sector and could be implemented with little complexity in reporting.

The change to a cash accounting basis was favored in the NFIB Mandate by 70% of the firms. In the current study, 74.7% of the firms felt it would be helpful, but 17.1% expressed no opinion. This no-opinion response leaves a large group of firms who need information and/or training to determine which way to move. Are these changes the most desirable alternative? The following section looks at the relative rankings of the proposed changes and offer a review of the comments from the respondents.

**Impact of Proposed Tax Changes on Small Businesses**

Numerous reports, studies and barbershop conversations revealed frequently mentioned tax changes that could benefit small firms. This study condensed those changes and asked small business people if they felt the changes would help in their firm.

An understanding of who would benefit most from changes in tax policy was considered a desirable objective. The frequency of responses is shown in Table 4 to illustrate the range of responses. Changes which were judged extremely helpful by a majority of the respondents included statements:
### Proposed Changes in Tax Policy

**PART III**

As a small business person, please rate the following proposed changes to current tax law in relation to their possible impact on small businesses. **CIRCLE** the appropriate answer for each question.

<table>
<thead>
<tr>
<th><strong>Proposed Change</strong></th>
<th><strong>Extremely Helpful</strong></th>
<th><strong>Somewhat Helpful</strong></th>
<th><strong>Not Very Helpful</strong></th>
<th><strong>No Opinion</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Simplify reporting procedures and liberalize deposit requirements for payroll taxes.</td>
<td>849 63.6</td>
<td>356 26.9</td>
<td>64 4.8</td>
<td>65 4.9</td>
</tr>
<tr>
<td>2. Liberalize depreciation rules for plant and equipment.</td>
<td>616 46.2</td>
<td>450 33.8</td>
<td>108 8.1</td>
<td>158 11.9</td>
</tr>
<tr>
<td>3. Simplify depreciation rules for plant and equipment.</td>
<td>607 46.4</td>
<td>460 35.2</td>
<td>92 7.0</td>
<td>149 11.4</td>
</tr>
<tr>
<td>4. Make tax regulations and laws apply on an equal basis regardless of business form (individual-partnership-corporation).</td>
<td>582 44.2</td>
<td>285 21.7</td>
<td>190 14.4</td>
<td>259 19.7</td>
</tr>
<tr>
<td>5. Institute a &quot;reward&quot; system of discounts for timely tax payments and elimination of civil penalties for late payments.</td>
<td>709 53.3</td>
<td>345 26.0</td>
<td>185 13.9</td>
<td>90 6.8</td>
</tr>
<tr>
<td>6. Reduce number of tax filings for various items (e.g., withholding FICA) to a less frequent basis.</td>
<td>746 56.0</td>
<td>342 25.7</td>
<td>190 14.3</td>
<td>55 4.1</td>
</tr>
<tr>
<td>7. For small firms, eliminate taxes on inherited business property passed to related parties.</td>
<td>977 72.9</td>
<td>202 15.1</td>
<td>55 4.1</td>
<td>107 8.0</td>
</tr>
<tr>
<td>8. For all small firms, allow cash accounting for tax purposes.</td>
<td>676 51.3</td>
<td>309 23.4</td>
<td>108 8.2</td>
<td>226 17.1</td>
</tr>
<tr>
<td>9. Extension of the general jobs tax credit for small business rather than the recently passed targeted job credit.</td>
<td>505 38.2</td>
<td>332 25.2</td>
<td>94 7.1</td>
<td>389 29.5</td>
</tr>
<tr>
<td>10. Permit small business corporations to accumulate earnings without full taxation on subsequent distributions.</td>
<td>886 66.7</td>
<td>235 17.7</td>
<td>41 3.1</td>
<td>167 12.6</td>
</tr>
</tbody>
</table>
7. Elimination of taxes on inherited property passed to related parties (72.9%).

10. Accumulation of earnings without full taxation on subsequent distribution (66.7%).

1. Simplify reporting/liberalize deposit requirements for payroll taxes (63.6%).

6. Reduction of number of tax filings (i.e., FICA) (56.0%).

5. Reward system for timely payment (53.6%).

8. Allow cash accounting for tax purposes (51.3%).

While "any change," of the types presented to the respondents was generally favored, three items had larger negative opinions than the others. These included the following three statements:

4. Make tax regulation apply on an equal basis regardless of form (14.4%).

6. Reduce number of tax filings (14.3%).

5. Institute reward system (13.9%).

In addition, three other statements had a higher percentage of "no opinion" responses than the other changes. These "no opinion" responses were to the following statements:

9. Extension of general jobs tax credit (29.5%).

4. Make tax regulation apply on an equal basis regardless of form (19.7%).

8. Allow cash accounting for tax purposes (17.1%).

The identification of the response categories related to each statement presents some interesting conflicts for policy makers. Statements 5 and 6 are seen as extremely helpful and not very helpful to the largest number of firms. For Statement 4, a rather large group (34.1%) would not be seen as
supporters of such a change despite the generally positive nature of "equality" implied in the statement.

In addition, the jobs credits and cash accounting changes appear to need broader discussion and information dissemination if these changes are to be instituted.

The smaller firms appear to have more difficulty in taxes in general. Most do not use a certified public accountant, and as seen in Statement 5 a "reward" could be an incentive to pay more attention to tax payments. Similarly, cash accounting (Statement 8) provides a one system approach which appears desirable to the smaller categories of firms.

The jobs credits were not extensively used by the smaller firms, but they see the general tax credits as less cumbersome than the targeted approach.

The larger firms appear in general to be able to take advantage of more alternatives in tax planning. They spend more money having taxes prepared and are more likely to have a CPA assisting them. The depreciation statements (2,3) therefore, provide benefits to the larger firms. Also, they could have more to depreciate and this is part of the benefit, especially for liberalizing the rules.

Differentiation based on other profile characteristics is feasible if policy makers wanted to accurately determine who would benefit the most from changes. Periodic sampling could be conducted when changes are occuring.

One admittedly non-scientific approach to see in more depth what the respondents felt without our guidance was an open-ended question which asked for "the most important changes in tax laws you feel are needed to promote the development of small business firms like yours." The results are summarized in Table 5. Specific comments are also highlighted in the
following sections.

Table 5
Most Often Mentioned Changes
(based on open-ended response)

<table>
<thead>
<tr>
<th>Change</th>
<th>Count</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reduce payroll (FICA) taxes</td>
<td>196</td>
</tr>
<tr>
<td>Reduce taxes in other areas</td>
<td>181</td>
</tr>
<tr>
<td>Simplify/reduce regulations or forms</td>
<td>143</td>
</tr>
<tr>
<td>Provide incentives/credits</td>
<td>70</td>
</tr>
</tbody>
</table>

The respondents were often exceptionally candid. The flavor of their responses concentrated on three points: reduction of taxes, simplification of paperwork, and incentive/credits,

**Reduction of Taxes.** The major concern with the cost of payroll taxes and reduction in general produced the following comments:

1. "taxes"

2. "If it doesn't stop soon there will be no small business left, then ask Uncle Sam who's going to pay the way? Big Corp? Hell no!!! We need help now."

3. "... The tax bite is far too great and we should be given relief. Congress had little trouble in increasing salaries and allowances for their cost of living increases. Why not the taxpayer?"

4. "Payroll taxes prohibit hiring!
   Payroll taxes prohibit expansion!
   Payroll taxes prohibit salary increases!
   Payroll taxes contribute mightily to new business failures!
   Payroll taxes contribute mightily to income tax evasion and/or fraud!
   Payroll taxes are a very poor investment!
   (Yes, originally they were investments in one's country and one's later years)."

5. "I'm ready for another Boston Tea Party but instead of tea we use bureaucrats!! I am sick of it."

6. "... Dividends paid by a small corporation should be entered as an expense to eliminate double taxation. Estate tax is a shame." (P.S. The spots on the page are tears and sweat!)
7. "Reduce the general tax levied on small businesses. Large corporations have so many "loop holes" to reduce taxes, where small businesses can only "go by the books." By the time you pay all the taxes (Employee and federal) there is no capital left to expand."

8. "Give us a break to get started. Why not reduce the taxes for the first years in business so we can build it?"

**Simplification / Reduction of Paperwork.** The tone here was not as strong, possibly because of the "hidden" tax nature of these items but the comments were revealing.

1. "What we need from the government is salad lettuce alone."

2. "Simplicity - I know you would rather me be more specific, but I work too hard ... There's no way on earth for me to know for sure that I am not in trouble about taxes every time I turn around."

3. "Let every business pay a percent of total gross sales. This would rid us of expensive lawyers, CPAs; and be fair for everyone."

4. "A recognition of the fact that small businesses do not have the resources available of the large businesses to comply with federal requirements."

5. "Change reporting procedures ... Small businesses just don't have time."

The first areas of changes are in areas of expansion and resources available to small firms.

**Provision of Incentives and Credits.** Several respondents felt there were no funds available for small business expansion and that current policies did not offer an internal source of financing. Their comments were often more precise but as in the first comment, it is obvious for one firm at least that survival wasn't possible.

1. "High taxes, inflation, and government record keeping have temporarily forced me out of my small business and into the employ of a large company. I don't feel I am qualified to answer your questions."

2. "Tax credits are needed for employment expansion similar to investment tax credit for big manufacturing companies."
3. "... innovative and creative opportunities exist to help the small business conserve "early need" cash from operations by relaxing "deposit requirements."

4. "No tax on undistributed capital profits."

5. "How will my son ever get into business when I die if we have to pay all we ever got in inheritance taxes?"

--Will the first person come back to small business?

--Will any business change hands and be family businesses?

--Can growth occur?

These obvious questions from the comments indicate more frustration than seen in any other research this author has conducted. Specific action must be taken to protect the segment which employs the people, provides the services and keeps the system going. The first comment about "where will Uncle Sam be . . ." was strong in most of the responses.

5. CONCLUSIONS AND RECOMMENDATIONS FOR ACTION

One of the most obvious findings is that people are willing, even eager, to respond as evidenced by the open-ended question discussed earlier. This eagerness takes on a tone of "nervous energy" and concern as you read the comments. An urgency is clear and evidenced in the exceptionally high levels of agreement with the statements in Table 3 and the sense of nearly any change at this point has a chance of being better than what exists now. This report was never intended to "determine the cost effectiveness for the federal government of changes in tax policy." It simply reports what the small business people representing the small business populations of the eight southeastern states are concerned with and want changed.

Reduction of taxes, specifically payroll taxes, is the primary concern. Payroll taxes seem to sap the strength of a large number of firms. One reason employment taxes became such a burden is because of changes in
the dependency ratio (the ratio of non-workers to workers). In 1945, it was 35 to 1, today 3.2 to 1 and it is predicted to fall to 2 to 1 after the year 2000. Recognition of the impact is critical to the respondents. The small business recommendation is to reduce both the cost burden and reporting requirements.

The second major area of concern expressed in all sections of the study was related to simplification and a reduction of paperwork. Several recommendations are related to this concern.

1. Initially, Congress should stop using only lawyers to finalize tax regulations. Small business advocates clearly felt the people affected by the regulations should help write them. Current committee hearings are often a joke to individual business persons. Comments such as "How can I afford to fly to Washington to have my say; I am hurting now," are common.

2. A second recommendation relates to simply thinking about the impact of regulations on the firms. The job credit example is one which is obvious. Other tax credits may take too much outside assistance.

3. The "tax impact study" is one recommendation which could assist policy makers in their deliberations. Business firms conduct environmental impact statements, why shouldn't government conduct "tax impact" studies to learn the full cost of compliance to the firm and to the government. It appears that some taxes are more costly to administer and simplification could be desirable to both parties.

4. Numerous respondents asked for more tax assistance. Also, 78.6% of the respondents felt current advisory services do not give enough help to small business. The recommendation would be to contract with outside sources to provide a "no-risk/no-fault" advisory service to allow firms to determine whether they are in compliance with current regulations. A similar program exists for OSHA related regulations in at least one major university.
extension of the concept does not appear to be a radical departure.

5. The cash accounting recommendation appears to be one favored by small firms who understand it. The single system argument is persuasive when the data in Table 1 concerning the lack of professional assistance in accounting record keeping is considered.

The final area of concern was with developing expansion capital. In general, respondents felt small firms were at a disadvantage in attracting and generating capital.

6. One recommendation is to develop industry-based, risk-adjusted, long-term, capital-gains rates to adjust for differences in risk of small and large firms. Simply put, higher risks need higher returns to attract capital.

7. Allowing reinvestment of fixed levels of profits with deferred taxation has been proposed to generate capital. In addition, this would reduce the higher tax burden small proprietorships face. The discussion in Section 3 supported this view and this is one way to partially resolve this differential. A related proposal not investigated in this study, but with merit is the deferring of capital gains on the sale of a business if the proceeds are reinvested in another small business within 18 months. The advantage would be the use of nontaxed money for 18 months, but more important is the "new" capital this generates so that the smaller firms can expand.

8. The final recommendation for developing expansion capital is to eliminate inheritance taxes on inherited business property passed to related parties. This change is another "new" source of capital and also eliminates many of the valuation problems in family and closely held firms.

To generate funds for the payment of taxes on the estate, there exists two major alternatives. The first alternative is to sell the business to a third party. Current tax law favors disposing of a small business
through transactions with larger businesses, thus lessening the chances for the survival of the independent small business. The second alternative, borrowing to pay the estate taxes, may put the small business in a precarious financial position resulting from the cost of borrowing and the repayment of borrowed funds. The estate tax provisions in the law are thus another method by which our taxing system discourages the maintenance of small business independence. The respondents felt this change would be helpful in 88% of the cases.

Changes and improvement in existing tax policy are based on a rethinking of the role of the small business in the economy. In addition, an understanding of how taxes affect the operations and growth of small firms is needed. The tax concerns of small businesses are so great that, if one issue could organize them, taxes appears to be the one.
REFERENCES


U.S. Senate Committee on Small Business, Impact of the Administration's Tax Stimulus Package on Small Business and Examination of Employment Tax Credit Alternatives, 95th Congr., 1st Session.

THE EFFECTS OF EXISTING FEDERAL LAWS
AND REGULATIONS ON SMALL DOWNTOWN
BUSINESSES IN THE SOUTHEAST:
EVALUATION AND RECOMMENDATIONS

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1. INTRODUCTION

A recent 32-page U. S. Department of Housing and Urban Development (HUD) report stated, "The urban fiscal crisis is not over--the future of our cities still demands the priority attention of government at all levels." (8) This report was in response to a report by Touche Ross and the First National Bank of Boston which concluded, after a study of 66 medium-sized cities, that many aging cities had lower tax and debt burdens and spending levels than did some of the younger growing cities. In other words, as stated in a Wall Street Journal article of April 13, 1979, ". . .you couldn't measure a city's budget needs (and its needs for federal aid) simply by looking at the sort of socioeconomic statistics that Washington favors. . ." (8) If the conclusions of this "fiscal stress" report are correct, then there are some major flaws in HUD's funding formula approach to providing aid to ailing urban centers in this country.

Charleston, West Virginia, after being granted one of the largest HUD Urban Development Action Grants to date, to aid its downtown, suddenly found itself faced with a major regional shopping center developing on its
Outskirts. This center threatened to further weaken Charleston's downtown despite its federally assisted redevelopment program. Upon further investigation, it was revealed that the Appalachian Regional Commission was assisting the development of this regional center by constructing a main highway interchange to provide access to the center. Is this coincidental conflict of purposes between federal agencies just a fluke or are there more?

Federal government involvement in aiding sagging central cities began in earnest during the rapid suburbanization period following World War II. Such programs as Urban Renewal, which spend billions of tax dollars to clear center city areas of "urban blight and decay," encouraged rapid suburbanization and central city abandonment. Other programs such as federal loan programs and mortgage guarantees to G.I.'s and developers encouraged urban flight also.

After over 30 years of such practices, the mayor of Burlington, Vermont (who has recently waged a successful fight to protect his downtown business district from the onslaught of a suburban regional mall) was quoted at a recent Georgia Downtown Development Association Conference as saying, "...we must keep our downtown healthy so we don't have to go to Washington to get the taxpayer's money to bail the cities out..."(6)

How can officials at the local level know what assistance is available to them from the federal government in this day of pervasive federal laws and regulations? The most comprehensive source of information is the Catalog of Federal Domestic Assistance, which is published annually by the Office of Management and Budget. It contains over 1,000 different federal programs that range from assistance for the study of volcanic eruptions to assistance for the development of fallout shelters. Determining which of these 1,000 plus programs can be related to improvements in downtown...
businesses can be a time-consuming task for local officials.

It is important to realize the distinctions between the different kinds of assistance that are available through the various federal programs. Approximately 27 of the 1,000 programs provide for five different types of assistance according to a study entitled, "Financing Downtown Action." (4, pp. 50-51) First, there are project grants or formula grants. These are dollar grants made to an eligible recipient for a particular project or group of projects either on a matching or non-matching basis. This means that under some programs, in order to receive grants, the applicant must put up a certain share of the total project cost on his own. Under other programs, no local funds are required. Loan shares can be in cash or in non-cash improvements to the project area.

A second type of assistance is direct loans. Depending upon the programs, direct loans can be made to either the public or private sector, and to either profit or non-profit organizations for the purpose of executing an eligible project. Interest rates are related to the rates that the U. S. Treasury has to pay for borrowed money. Therefore, these rates are reviewed, and sometimes revised, on a quarterly basis.

The third type of assistance is through guaranteed or insured loans. It is much easier to secure financing when the federal government is guaranteeing or insuring the loan. Because the federal government is backing the loan, there is less risk involved for the lender, and thus interest rates will tend to be lower.

The fourth type of assistance available is not monetary assistance, but rather technical assistance or advisory services. Under a program known as Economic Development Administration (EDA), the federal government assists local governments and other public and private organizations in
shaping projects and programs that are designed to foster economic growth and development in economically depressed areas—including downtowns.

The last type of assistance to be mentioned concerns the sale, donation, or exchange of surplus property or goods owned by the federal government. The disposal of federal surplus real property handled by the General Services Administration makes surplus federal property available to states, local governments, non-profit institutions, and private individuals. Compensation can range from no cost to fair market value, depending upon the use to which the property will be put.

From this outline of the various types of programs available, it is clear that the federal government has not stood idly by as the cities have called for aid to save their ailing downtown small businesses. Program after program has been promulgated in an attempt to find the right solution. Urban Renewal, Model Cities, Community Development Block Grants, 701 Planning Assistance, Farmers Home Administration, Small Business Administration, and now Urban Development Action Grants have all attempted to help in this regard.

In his National Urban Policy Report of 1978 (3), President Carter pledged that national urban policy-making had entered a new phase, "...now departments and agencies throughout the federal government are taking steps to reform existing programs and to develop proposals for legislative action. State and local government officials are preparing themselves to enter into the partnership opportunities that are being opened..."(3, p. 127)

What is the true purpose for the preponderance of federal programs to assist ailing downtowns? Is it not to help downtown business in general and small downtown businesses in particular which are the very heart of downtown? In this day of Proposition 13, citizens are seeking ways to
uncomplicate their lives and rid themselves of the burdens of unnecessary government taxes and regulations. As a result, today's cities face the threat of losing tax dollars which have been available to promote downtown revitalization.

Some believe the federal government is doing too much to assist ailing cities. Some believe they are doing too little. Some want to know exactly what the federal government is doing to assist cities. It was reported on the CBS "Thursday Morning News" program on May 24, 1979, that in Cloud Lake, Florida, the federal government had come to the aid of this supposedly ailing city by sending the city a check to aid in its recovery. After intense investigation it was discovered that the President had declared Cloud Lake, a city of 136 people near Palm Beach airport, a major disaster area. City officials called Tallahassee (the state capitol) for clarification. None was provided. Finally, they called Washington and learned the check was to aid in their recovery from a severe crop freeze in 1977. The problem was the city had no crops. The federal officials then assured the city the check was to aid local businesses in recovering from the effect of crop failures in adjacent counties. The main business in Cloud Lake was an adult movie theater which had not incurred any appreciable loss of income from the "freeze." The city was in a quandry as to what to do, but decided to return the money to Washington. The check was for $22.61. Is this an example of good intentions to aid small downtown businesses by the federal government, or is it an example of mismanagement by a government which has lost touch with reality?

The President's "National Urban Policy Report of 1978," alludes to an awareness that conflicts exist in current federal programs which have tended to contribute to continued urban sprawls. The "Policy" states that federal
action should be coordinated. . ." if we do not, development undertaken or assisted by both levels of government (federal and state) will encourage land use patterns that result in pollution, clogged highways, under-used public services and utilities, and wasteful use of scarce land resources." (3, p. 127)

From the President's "Urban Policy" statements as well as statements from other levels of the federal government, we detect signs that the federal government is aware of its involvement in the demise of the small downtown business. Richard Fleming, HUD's General Deputy Assistant Secretary, Office of Neighborhoods, Voluntary Associations and Consumer Protection, stated at a recent Georgia Downtown Development Association conference that, "The Carter administration recognizes both the severity of the economic problems of urban areas and the real limitation on the federal government's resources." He went on to state that, "We can no longer allow federal aid to localities to simply be broadly and randomly dispersed as it has been in the past." (5)

Mr. Fleming stated, "...that a new urban partnership is emerging in this country, and that it is bringing positive and substantial benefits to cities. . .What the Carter administration has sought to do since 1977 is to reorganize community and economic development aid in such a way that successes. . .becomes a national trend and not just random examples of creative local leadership." (5)

"Regulations and operating procedures in the federal establishment are being streamlined to make joint development projects more attractive to cities and their investors. HUD, EDA, and SBA have all pledged their commitment to working towards this goal and to providing technical assistance to cities in packaging loans and development projects." (5)
Since laws and regulations affecting the introduction and development of small business in downtown areas are promulgated in several agencies of the federal government and little or no evidence exists to indicate coordination between these agencies, this study will analyze the effects of existing laws and regulations at the local level. The purpose of this research is to:

1. Identify critical laws and regulations affecting the introduction and development of small downtown businesses in the Southeast either positively or negatively.

2. Identify the agency of the federal government from which the laws and regulations come.

3. Discuss areas in which existing laws and regulations conflict.

4. Suggest changes to improve existing federal laws and regulations.

5. Discuss the implications of existing federal laws and regulations on the long-run well-being of small downtown businesses in the Southeast.

2. METHODOLOGY

In order to obtain the best possible information for the purposes of this research, it was decided that knowledgeable insiders, individuals privy to the inner workings of city government, would be queried. The logic was that those who stand to benefit most or suffer most from federal laws or regulations should be most familiar with the intricacies of those laws and regulations. In effect, there were two primary groups suitable for study: individuals in city governments; and businessmen owning and/or operating small downtown businesses.

It was decided that individuals in city government would be more likely to have at their disposal the kinds of information needed for this study. Businessmen who own and/or operate small downtown businesses must spend most of their time managing the affairs of their businesses.
Additionally, they do not have sufficient excess resources to hire individuals to monitor the activities of the state and federal government. They are forced to rely upon city governments (or groups like the Chamber of Commerce) to protect their interests by monitoring the activities of the state and federal government and providing information which might affect the well-being of their firms.

City governments, by their very nature, develop expertise in dealing with other governments. The trend toward bigger government, at both the state and federal levels, has increased the burden on city governments. It has forced them to create positions designed for monitoring state and federal government activities and to develop people to fill them. Cities not following the activities of the state and federal government are not in a position to know when funds are available, from what source they come, and what must be done to get them. Competition among cities for government dollars is keen. Given the situation as it exists today, city governments choosing not to follow state and federal government activities will suffer considerably in relation to city governments who do. More importantly, citizens and businessmen in cities whose local governments choose not to follow state and federal government activities suffer in the sense that resources which could be made available to them are not made available to them.

Not every city is large enough to justify the expenditures required to monitor effectively the activities of the state and federal government. For this reason, it was decided that the focus of this research should be on cities whose population was greater than or equal to 30,000 according to the 1970 census. There are 83 cities in the eight Southeastern states who meet this criterion.
The names of the mayors of the 83 cities were obtained and they were contacted via the United States mail. The purpose of this research and its importance was explained to each mayor, and they were asked to delegate to the "most knowledgeable person" in their city the responsibility for completing the questionnaire. The purpose for not specifying the person who should complete the questionnaire was that mayors, like business managers, tend to rely on individuals who have specific knowledge and expertise rather than people who hold certain positions. It was believed that by following this procedure, the most reliable information available could be obtained. Additionally, this procedure did not limit the mayor to people directly affiliated with city government. If the director of the local Chamber of Commerce was the best person for the job, the mayor was free to ask for his assistance.

The questionnaire was short in terms of the number of questions asked, but it required considerable time in thought before it could be completed. It was pre-tested on five knowledgeable individuals prior to mailing. As a result of the information obtained from the pre-test, the mayors were informed about the time involved in completing the questionnaire and the depth of knowledge required for its satisfactory completion. Also, they were asked to use this information in deciding who should complete the questionnaire.

The persons completing the questionnaire were asked to identify specific federal government laws and regulations affecting the introduction and development of small downtown businesses in a positive or negative way. They were asked to identify any federal government laws and regulations conflicting with one another and acting to discourage the introduction and development of small downtown businesses, and they were asked to suggest
additions to or deletions of existing federal laws and regulations in order to encourage the introduction and development of small downtown businesses.

3. DESCRIPTION OF THE SAMPLE

As was stated previously, our sample consists of those cities in the eight Southeastern states whose population was equal to or greater than 30,000 according to the 1970 census. A list of the 83 cities in the Southeastern United States meeting these criteria for inclusion in this study is included herein as Table 1.

Of the 83 cities surveyed, a total of 13 responded (15.7%). Nine of the cities responding (10.8%) provided complete answers to most of the questions asked. Four responding cities (4.8%) answered no questions. Instead, they explained why they could not (or would not) respond. Their reasons for not responding are as revealing as the answers supplied by the other nine cities. An analysis of those responses will be presented in the following sections of this paper.

The average size of the 13 responding cities is 94,039 according to the 1970 census. The average size of the cities providing complete information was 1.58 times greater than the average size of cities who only explained why they would not respond. The average size of the cities in the two aforementioned groups is as follows:

- Average size of cities responding completely: 135,834
- Average size of cities giving their reasons for not responding: 85,903

Table 2 shows the eight Southeastern states included in the study, the number of cities surveyed in each state, the percent of those cities surveyed from each state who explained why they would not respond, and the percent of those cities from each state who responded in either way.
### TABLE 1

**States and Cities**

<table>
<thead>
<tr>
<th>Alabama:</th>
<th>Florida (Cont'd):</th>
<th>Mississippi (Cont'd):</th>
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<tbody>
<tr>
<td>Anniston</td>
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<td>Jackson</td>
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<td>Bessemer</td>
<td>Titusville</td>
<td>Meridian</td>
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<td>Birmingham</td>
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<td>W. Palm Beach</td>
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<td>Florence</td>
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<td>Gadsden</td>
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<tr>
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<td>Albany</td>
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<tr>
<td>Coral Gables</td>
<td>Athens</td>
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<tr>
<td>Daytona Beach</td>
<td>Atlanta</td>
<td></td>
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<td>Fort Lauderdale</td>
<td>Augusta</td>
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<td>Gainesville</td>
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<td>Hialeah</td>
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<td>N. Miami</td>
<td>Kentucky:</td>
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<td></td>
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<td></td>
<td>Gulfport</td>
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<td></td>
<td>Hattiesburg</td>
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</table>

| North Carolina:|                           |                           |
|                | Asheveille                 |                           |
|                | Burlington                 |                           |
|                | Charlotte                  |                           |
|                | Durham                     |                           |
|                | Fayetteville               |                           |
|                | Gastonia                   |                           |
|                | Greensboro                 |                           |
|                | High Point                 |                           |
|                | Raleigh                    |                           |
|                | Rock Mount                 |                           |
|                | Wilmington                 |                           |
|                | Winston-Salem              |                           |

| South Carolina:|                           |                           |
|                | Charleston                 |                           |
|                | Columbia                   |                           |
|                | Greenville                 |                           |
|                | Rock Hill                  |                           |
|                | Spartanburg                |                           |

| Tennessee:    |                           |                           |
|              | Chattanooga                |                           |
|              | Clarksville                |                           |
|              | Jackson                   |                           |
|              | Johnson City              |                           |
|              | Kingsport                 |                           |
|              | Knoxville                 |                           |
|              | Memphis                   |                           |
|              | Nashville-Davidson        |                           |
TABLE 2

<table>
<thead>
<tr>
<th>States</th>
<th>Cities Included in Study</th>
<th>Cities Responding Fully</th>
<th>Cities Saying They Would Not Respond</th>
<th>(B + C)</th>
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</thead>
<tbody>
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<td>12</td>
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<td>8.3%</td>
<td>1</td>
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<tr>
<td>Florida</td>
<td>23</td>
<td>3</td>
<td>13.0%</td>
<td>6</td>
</tr>
<tr>
<td>Georgia</td>
<td>11</td>
<td>1</td>
<td>9.1%</td>
<td>2</td>
</tr>
<tr>
<td>Kentucky</td>
<td>6</td>
<td>-</td>
<td>0%</td>
<td>-</td>
</tr>
<tr>
<td>Mississippi</td>
<td>6</td>
<td>-</td>
<td>0%</td>
<td>-</td>
</tr>
<tr>
<td>North Carolina</td>
<td>12</td>
<td>1</td>
<td>8.3%</td>
<td>1</td>
</tr>
<tr>
<td>South Carolina</td>
<td>5</td>
<td>-</td>
<td>0%</td>
<td>-</td>
</tr>
<tr>
<td>Tennessee</td>
<td>8</td>
<td>3</td>
<td>37.5%</td>
<td>3</td>
</tr>
<tr>
<td></td>
<td>83</td>
<td>13</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The 13 responses, when grouped according to the position of the person completing the questionnaire or explaining why it would not be completed, revealed the following:

A. Five titles were represented:
   1. City Manager
   2. Administrative Assistant to the Mayor
   3. Director of the Downtown Development Authority
   4. Planning Director
   5. Director of Community Development

B. Of the nine complete responses:
   1. Seven came from persons holding the position of Planning Director
   2. Two came from persons holding the position of Director of Community Development

C. Of the four explanations for not responding:
   1. Two came from City Managers
   2. One came from an Administrative Assistant to the Mayor
   3. One came from the Director of the Downtown Development Authority

4. PRESENTATION OF FINDINGS

There were so few responses to the questionnaire that it is appropriate to present most of the comments made by the respondents. By so doing, the reader will be able to more fully grasp the implications of the manner of
thinking characterized by the respondents. If, in fact, the reasoning they employ typifies the reasoning of most individuals in city governments in the Southeast, one can easily understand why the trend toward increased federal government involvement in business is gaining momentum. Their responses indicate a reliance on the federal government for financial assistance rather than help in building a solid economic base.

From the Complete Responses

Of all the laws and regulations emanating from the federal government, those administered by the Small Business Administration (SBA) received the most attention. Seven of the nine respondents referred to SBA loans and loan guarantees, and all seven agreed that the effects of the programs administered by the SBA were positive. The following are comments made by the respondents:

* They enable marginal firms to survive until they stabilize.
* They make funds available on a public and private basis to small businesses which cannot secure normal private sector funding.
* They enable money to be funneled to small and medium sized businesses whose "track record" is not impressive and whose assets are not great enough for private sector funding.
* They are used to "bail out" or help solidify companies on the verge of collapse due to under capitalization.

The second most frequently mentioned program was the Community Development Block Grant Program (CDBG) administered by the Department of Housing and Urban Development (HUD). Four of the nine respondents referred to the program. Two felt that its effect was positive and two felt that its effect was negative. Following are the comments of those who believed the effects of the CDBG Program are positive:

* They show the commitment of the local and federal government to the area, and they encourage retention of small businesses.
* The use of CDBG funds to acquire various parcels in a two block area of downtown will certainly provide a positive effect toward the overall improvement picture in the downtown area. These two blocks were in a deteriorating stage, and now the land can be redeveloped.
This may lead to the introduction of some new small businesses.

The respondents who believe the CDBG Program has negative effects made the following comments:

*CDBG monies cannot be used as "seed" money for private business development in the downtown area.

*The current regulations make it virtually impossible for discretionary CDBG funds to be expended to upgrade and improve the amenities of the infrastructure in the central business district.

Two respondents identified the Tax Reform Acts of 1976 and 1978 and said that both Acts have positive effects on small businesses in their cities. One respondent said of the Tax Reform Act of 1976:

*It allows one to deduct qualified rehabilitative expenses from the gross income of a property to reach taxable income before the taxes are calculated.

The provision of the Act to which the respondent refers deals with historic preservation. It is not certain whether the respondent intended the aforementioned statement to mean that historic preservation will result in a more scenic downtown and thus attract new businesses, or encourage owners or managers of older firms to refurbish their dwellings.

Another respondent was more specific. He said the following about both the Tax Reform Acts of 1976 and 1978:

*Historic preservation incentives encourage the rehabilitation of small downtown structures which otherwise would be obsolete and not competitive with newer suburban structures.

The Department of Housing and Urban Development's Urban Development Action Grants (UDAG) were mentioned by two respondents. Both saw the effects of the grants to be positive and negative. One respondent said the following:

*The program has a positive effect in that it brings federal funds and private funds together. This concept is a sound one. Its effect is negative in that many cities with seriously deteriorated central business
districts are precluded from participating in the program because their overall economies do not meet distress criteria.

One respondent was critical of the interstate highway system administered by the Department of Transportation. The following comment was made:

*The interchanges in suburban areas along interstate highways are a direct subsidy to suburban retail developments. They enable a developer to make a greater profit or offer rents at an artificially low price.

Concerning conflicting federal laws and regulations, the following comments were made:

*Recent guidelines issued by HUD have encouraged the spending of urban renewal funds in areas other than central business districts. This could affect the general condition of downtown areas which, in turn, could hurt the introduction and development of small downtown businesses. There may be a conflict between these HUD guidelines and the efforts of some cities to develop their central business district.

*Participation in the Community Development Block Grant Program (CDBG) as an entitlement city eliminates the possibility for 701 Planning Assistance. CDBG planning is normally oriented to planning for neighborhood housing. The CDBG Program as a source of funding for downtown improvement planning is lost. The 701 Comprehensive Planning Program is of upmost value to localities in developing the type of programs which support and encourage improvement of downtown businesses. The preclusion of entitlement cities under the CDBG Program from receiving 701 comprehensive planning assistance should be deleted.

*If a downtown area is designated for funding under the CDBG legislation because of identified needs of low income citizens of minorities, this designation limits the possibility of future construction of assisted housing. This type of construction would provide additional consumers for downtown business activities. The prohibition against construction of assisted housing in impacted areas should be substantially modified to allow for review on a case by case basis.

Several suggestions were made by the respondents concerning changes which could be made to improve existing federal laws and regulations. Some of them are listed below:

*HUD guidelines relating to the Housing Community Development Act of 1977, at least as interpreted in this region, have severely limited the use of CD funds for downtown economic development activities. It would be very helpful to our economic development efforts if more eligibility were allowed in the use of these funds. In the early years of the CD program, this city utilized more of the
funds for such downtown renovation. The effect on many small CBD firms was very positive.

* Often local businessmen and local leaders do not and cannot take advantage of available programs because of lack of information in regard to program content or availability. Legislation should require increased responsibility on the part of the administering federal agency to disseminate accurate information about possible program benefits and requirements. This type of action would increase competition for available funds and result in better proposals.

* The federal government should centralize the application process for downtown business economic development activities as much as possible. This process would route to the appropriate department or agency the request for funding.

* Regulations covering the discretionary CDBG Program should be modified to allow for some expenditures to upgrade infrastructures and amenities in central business districts. This could in turn encourage investment by downtown businessmen who might be convinced the local government is committed to the downtown business district.

* Urban Development Action Grants (UDAG) regulations should be modified to make cities with healthy overall economies eligible for the UDAG Program for their distressed downtown areas. The idea of combining private and local funds with federal funds is a good one, but many communities with deteriorated central business districts are unable to qualify for the program because their overall economies are in relatively good shape. This change would help make the funds which individual shop owners have for investment stretch further as well as encourage collective action by downtown merchants and property owners.

* In order to preserve one of our most important renewable resources (the owner-occupied dwelling), the Tax Reform Acts of 1976 and 1978 should be amended to encourage the rehabilitation of these structures; just as it encourages the preservation of income producing properties such as rental homes. This addition to the Tax Reform Acts of 1976 and 1978 would encourage the conservation of many of our residential neighborhoods that are encouraged to deteriorate because of our existing property tax structure.

From Explanations Why They Would Not Respond

* The questions contained in the questionnaire are not questions which can be answered by anyone within the city government. We simply are not involved with the development of small downtown businesses and have no knowledge about the impacts of various federal programs on the development of such businesses.

(A City Manager)
*We have chosen not to respond to the questionnaire because, after careful review, it was found that laws and regulations emanating from the federal government have neither positive nor negative effects on businesses located in the downtown area.

(An Administrative Assistant to the Mayor)

*Although I commend you for your study, my judgment is that the information you desire cannot be obtained unless a considerable investment in interview time is made with individual proprietors and their accountants. Unfortunately, our staff is not available for this purpose.

(A Director of a Downtown Development Authority)

5. DISCUSSION

The data generated by this study is not sufficient to enable one to draw definitive conclusions about the effects of existing federal laws and regulations on the introduction and development of small downtown businesses. However, several questions are raised. For example, why did the respondents focus their attention almost exclusively on federal subsidies to businesses and to cities for improving existing conditions? Why was there no mention of incentives the government could provide to encourage businessmen to increase their investment? William G. Miller recently proposed that businesses be allowed to accelerate the depreciation of capital. This proposal, if accepted, would provide a strong stimulus for businessmen to make substantial investments in modernization and other improvements.

The Government's Plan

According to the President's National Urban Policy Report of 1978, the federal government intends to "support the development by urban localities of comprehensive metropolitan development strategies aimed at eliminating sprawl and revitalizing central cities." (3, p. 126) To implement this strategy, they will "use transportation as an incentive program to leverage
public and private urban revitalization activities and make urban transportation programs more effective tools to accomplish improved transportation and broad economic, environmental, and social goals." (3, p. 126)

In order to discourage urban sprawl and its accompanying effect on small downtown businesses, the federal government states that their efforts should encompass:

- "Use of federal and state construction, transportation, water and sewer programs in existing urban areas."
- "Removal of federal and state tax, business and insurance regulations favoring decentralization."

With the help of the federal government, urban sprawl has and does occur. Lawrence A. Alexander, director of the Downtown Research and Development Center states that, "There have been two main problems in downtown retailing (accepting suburbanization as a fact): these are first, that many downtown retailers did not flexibly adjust to the real changes going on. For many, this meant failure. Secondly, many retailers boarded their cars and moved out of town on what seemed the highway to riches. The result was that in many downtowns the real problem became the lack of supply of stores and merchandise. The old saying is that you can't sell from an empty cart." (2, p. 45)

Preventing urban sprawl requires targeting funds toward activities that tend to compact community development.

Respondents to this survey seemed genuinely concerned about downtown development and redevelopment and the positive effect the downtown's healthy condition should have on the whole community. Concern was expressed over the lack of information and coordination of the various programs available and how these programs fit into some type of policy that favors the protection of the health of downtown. It was suggested that the application process for
downtown economic development activities be centralized and coordinated in order to identify and route the request to the appropriate funding agency.

The reorganization of federal agencies for a more effective posture of cooperation as alluded to in the President's "Urban Policy Report" is either not working or not apparent to officials at the local level. The UDAG approach to downtown redevelopment has the potential to provide the most realistic approach to encouraging private sector initiative. But, as the surveys showed, even this approach is not available to all communities, due to an inadequate funding formula approach.

While aid to businesses in downtown areas is not specifically referred to in the President's "National Urban Policy Report of 1978," clearly it is included in an overall attempt to encourage compact development as opposed to urban sprawl. The government intends to accomplish its objective by creating what can be likened to a partnership between the federal, state, and local governments and entrepreneurs (i.e., UDAG).

One big factor in determining how well the President's urban plan works is the quality and quality of support businesses receive from local governments. This raises a critical question. Are cities managed well enough to allow them to provide this support? As a result of the 1976 amendment to the Federal Revenue Sharing Act, public accountants have been auditing cities (often for the first time). Their findings "put to rest two illusions: one, that the urban crisis is over; and two, that whatever crisis exists is not the result of hometown mismanagement." (7)

No matter how noble the intentions of the federal government, their plans can and will be thwarted if they rely on groups not capable of providing the assistance required of them. If the proposed "partnership" between federal, state, and local governments and business is to succeed, local governments must
demonstrate competence in running their cities first. Then and only then can they provide help to business.

Who Gets Financial Aid?

Determining which cities receive federal aid is a problem with which government must contend. Several respondents to the present survey said one big problem with the UDAG Program was that cities with good overall economies were precluded from participating in programs which could help their distressed areas. Another issue raised by the respondents involved the CDBG Program. Respondents said participation in this program precluded the opportunity to participate in 701 Planning Assistance. 701 Planning Assistance provides help to cities developing programs designed to support and encourage improvements in downtown businesses, and this is a purpose for which the CDBG Program exists.

Recently, "five of the seven wealthiest cities in Los Angeles County appeared on the U. S. Treasury list of the nation's most 'distressed' cities, thus qualifying for federal aid." (8) HUD received considerable criticism after this finding was made public. The editor of the Wall Street Journal alludes to a tremendous problem with subsidies and grants in general and subsidies and grants to cities in particular. They imply that subsidies and grants encourage one to live beyond one's means. It is common knowledge that the result of living beyond one's means is financial disaster. If, in fact, the government succeeds in developing the aforementioned "partnership," what will be the effect of subsidies and grants on downtown businesses?

HUD has provided a perfect example of the consequences of using funds designated for community development inappropriately to revitalize cities and reverse urban decay. They allowed New York City to divert $100 million in
federal community development funds to help pay expenses the city incurred after foreclosing on many apartment house owners for non-payment of taxes. The reason the taxes were not paid was that New York City's rent control laws made operating at a profit only a dream for many landlords. In effect, HUD demonstrated their approval of the inequitable situation (the New York City apartment house owners were in by subsidizing the city government while they took over the operation of what was once profitable, private enterprise).

Is There An Answer?

At least one major city has learned its lesson about relying on the federal government for support and is attempting to replace the federal government's dollars in their budget with dollars generated by private enterprise. New Orleans is not unlike other major cities in the United States. As the mayor of New Orleans, Ernest Morial, warned in his October budget message, "New Orleans depends more on federal funds than any other southern city and ranks close to the bottom of funds from its own resources." Naturally, the budget trimming in Washington hit New Orleans hard. Morial's response to the reality of federal cutbacks demonstrates sound economic logic. His administration is focusing on economic growth in the private sector.

Morial and business leaders in the city agree that growth should be targeted to benefit the city's poor. To this end, they are scanning the country searching for prospective labor-intensive businesses wishing to relocate in a sunbelt state. In order to attract firms, they are making efforts to upgrade the skill level of their work force. These efforts should have a twofold effect. One, the city will improve its economic base as industry moves into the city; and two, the city will be stronger because they did it for themselves instead of depending on the government to do it for them.
6. CONCLUSION

Perhaps the greatest conflict with respect to the federal government's attempts to aid small downtown businesses is in the attempt. The solution then is not in reworking existing federal programs to try to eliminate conflicts, but in the elimination of many programs. When someone helps open the cocoon, the butterfly dies because it misses the chance to use and develop its own muscle. So too, the small downtown business is weakened as it continues to have its "cocoon" opened by the overabundance of federal money made available to it.

The example offered by New Orleans and other cities who are trying to wean themselves from federal subsidies illustrates what should be the wave of the future. Job creation and capital formation is the job of business in the free enterprise system. Businessmen know how to do it, and they do it best.

The federal government's ability to create capital without producing a product is causing one of the greatest conflicts involving business in this country. Although programs such as UDAG offer one of the more palatable approaches to ailing downtown business development, the government's involvement as a stimulator or facilitator may encourage development that will not be able to make it on its own economic merits. This federal subsidy to development may produce a bubble whose eventual bursting may destroy many small businesses. The growing involvement of the federal government in the development of business can be compared to the federal government's involvement in the military-industrial complex, the farm industry, the railroad industry, the Corps of Engineers, and the postal service. In our zeal to see our cities and small downtown businesses remain healthy, we must beware of the danger of accepting something for nothing.
Private initiative and local initiative must be encouraged and fostered if our small downtown businesses are to survive.
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1. INTRODUCTION AND SUMMARY

For years the scope and impact of regulation of business by government have been increasing. At the same time, economists have been speaking out regarding the effects of regulation on the efficiency of the market economy. Commissions have been formed, conferences held, studies conducted, and articles written to analyze and debate this timely and important issue. And recently, a move toward "regulatory reform" has been prompted by concern with issues such as inflation, productivity, capital formation, and innovation.

If history provides any indication of the future, regulatory reform, whether in the form of deregulation by repealing existing legislation, reform of existing legislation, or reform within the regulatory agencies, is likely to be a relatively long-term process. In the meantime, an understanding of the financial impact of regulations on the business sector is essential to ensure that a reasonable, efficient, and stimulating business environment is maintained. My purpose is to examine the financial impact of Federal regulations on small business.

The reasons for examining the financial impact of Federal regulations on small business are threefold.

First, management of small business should, while complying with the regulations, strive to minimize the adverse financial impact of compliance. Attaining this objective can reasonably be expected
only with an understanding of the financial implications. Second, by understanding and recognizing the financial impact of regulations, government policymakers will be more effective in enforcing existing regulations. In other words, government policymakers will be in a better position to assess both the costs and benefits of enforcing existing regulations. Finally, with the trend toward regulatory reform, a knowledge of such financial implications will assist policymakers in developing new regulations that are effective while, at the same time, equitable.

In view of the preceding discussion, the material that follows will, in summary,

- examine the financial impact of regulation-induced expenditures in terms of the debt capacity of the firm,
- discuss how small businessmen can react to preserve the financial integrity of the firm, and
- assist policymakers in enforcing existing, as well as developing future, regulations in an effective yet equitable manner.

2. THE REGULATORY CLIMATE

In 1946, the United States Congress passed the Employment Act, a landmark in American socioeconomic legislation. This legislation committed the Federal government to pursue policies that promote the now-familiar economic goals of full employment, price stability, economic growth, and an acceptable balance of payments position. While this legislation is generally
recognized as being significant in establishing conventional economic policy in the post-World War II period, new social goals emerged during the mid-1960's and early 1970's, including cleaner air, safer and healthier working conditions, and equal employment opportunities. This list is far from being comprehensive. Over forty regulatory agencies exist today that have potential impacts on small business.

With this trend toward regulation, many parties have concluded that a conflict exists between "economic man," who has tended to be concerned primarily with producing goods and services, and "social man," who has tended to emphasize human rather than monetary values in life. In attempting to resolve this conflict, concessions will be made and both value systems will undoubtedly move toward a common ground. As these moves occur, many sectors of the nation will feel the impact. This attempt to compromise seems to be emerging via the movement toward regulatory reform. Compromise ideally infers that each participant should have an understanding of the position of the other participants. It is with this as a background that we examine the financial impact of Federal regulation on small business.

3. THE FINANCIAL IMPACT OF REGULATION

To understand and appreciate the financial impact of government regulation on small business, one must first recognize the financial status of the business sector in general. With the end of World War II, conditions were optimal in the United States for a rapid and prolonged era of economic growth. With a new wave of technology, economic activity expanded via more efficient methods of production, greatly improving existing products and developing new products. Innovation and new technologies resulted in increases in labor productivity and helped to satisfy an increased demand
for goods. In short, the end of World War II marked the beginning of twenty-five years of economic progress.

The business sector during this era equated progress with the automation associated with capital-intensive, labor-saving, and energy-intensive investments. In other words, more-expensive labor was replaced by machines that consumed larger quantities of relatively inexpensive energy. From a financial perspective, this meant that fixed costs for business increased while variable costs decreased as machines displaced labor and inexpensive energy was consumed to run the machinery. With this combination of higher fixed costs and lower variable costs, a higher level of output was required to break-even (where total costs equal total revenue). Once the break-even level of sales was exceeded, profits were greater than in the pre-automation period.

Several factors contributed significantly to the end of this twenty-five year period of rapid growth. One factor was the maturing of several of the technologies that originally started the era of growth. Another factor, beginning in the early 1970s, was the end of the era of cheap and abundant energy. Variable (energy) costs increased while fixed costs remained at high levels. Thus, an even higher level of output was required to break even.

Profitability Implications of Regulations. The emergence of some of the new products in the post-World War II period played a significant part in giving rise to one of the most important regulatory agencies, the Environmental Protection Agency (EPA). These products were developed on the basis of the profit motive when environmental regulations were not enforced or were nonexistent. Or as some would state, the new polluting technologies were more profitable than the older, less polluting technologies.
that were displaced. Examples of this technological change include the displacement of soap by detergents and the move away from natural fibers to synthetics.

Some economists have stated that these new products were representative of a market system that did not work. In other words, because these products were environmentally degrading, their market prices did not reflect the total cost to society. Because it was cheaper to pollute than abstain from polluting, the EPA was established to administer a system of controls.

Formed in 1970, the EPA is, of course, only one of numerous regulatory agencies that exist today. While not being an exhaustive list, other regulators that can have a significant impact on the business sector include Equal Employment Opportunity (EEO), Occupational Safety and Health Administration (OSHA), Department of Energy (DOE), Employee Retirement Income Security (ERISA), and the Federal Trade Commission (FTC). Rather than discuss any specific regulation or regulatory body in isolation, I intend to discuss the impact of regulations in general.

In terms of profitability implications, the commitment of funds to comply with regulations is significant on several counts. Such expenditures can represent a significant percent of the total cost of operating a business. Some advances have been made in calculating such costs for large companies. For example, the Business Roundtable published its Cost of Government Regulation Study in March of 1979. This study included 48 large companies and reported their direct incremental cost of complying with six federal agencies in 1977. Although reliable data do not exist regarding the exact cost of regulation to the small business sector, the scale effect of regulatory impact tends to discriminate against small versus large businesses.
This fact has long been recognized in economic impact statements conducted by regulatory agencies.

Depending upon the type of regulation, the costs of complying with regulations can be either variable or fixed. For illustrative purposes, it is more useful to use fixed costs to demonstrate the financial implications of regulation from the point of view of the firm. The process for evaluating capital expenditures, termed capital budgeting, typically entails an estimate of the potential return on each project. The proposed projects are arrayed in a priority ladder expressed in terms of their rate of return and are then compared with some acceptable criterion such as the cost of capital to make an accept-or-reject decision. Other things being equal, projects with equal riskiness are acceptable if the rate of return exceeds the cost of capital and funds exist to finance the project.

Expenditures to comply with government regulations are unusual additions to the typical capital budgeting system. It is generally accepted that, from the point of view of the firm, many expenditures to comply with government regulations are basically unproductive by nature. Given the unproductive nature of these assets, they will generate negligible, if any, cash inflows while at the same time necessitating significant cash outflows. The expenditure of such funds will typically depress the profitability of the firm. The extent of this depressing effect will depend on the ability of the firm to shift the costs to consumers through higher prices. In addition, if funds available to support capital expenditures are fixed, some projects that would have contributed to the profitability of the firm will have to be eliminated from consideration. Finally, several other costs that may or may not be measurable can have an impact on the profitability of the firm. These include investment
disincentives, construction delays, and a potential loss of the competitive position of the firm in general.

**Regulation and Risk.** In addition to their profitability implications, expenditures to comply with government regulations are likely to be unique with respect to risk. Expenditures to comply with EPA regulations can be used to illustrate the potential risks that government regulations can impose on a firm. Pollution abatement expenditures subject the firm to what may be termed "legislative risk," which is defined as the possibility that emission standards may be increased, either because of new legislation or by EPA interpretation of existing legislation, thereby rendering existing pollution abatement equipment legislatively obsolete and requiring the expenditure of funds for additional non-productive assets. Because of the nature of environmental legislation (i.e., legislative risk), it is therefore likely that sequential investments will be required rather than a one-time investment. Thus, from a financial point of view, consideration of expenditures to comply with existing abatement standards only is likely to be less than a complete analysis.

Probably the classic example of legislative risk today is the Water Pollution Control Act of 1972. This legislation established two dates, July of 1977 and July of 1983, for changes in standards for discharging wastes into U.S. waters. Although uncertainty is reduced with respect to the timing of the new standards, much uncertainty remains regarding the level of the standards. To illustrate, the law established July 1, 1977 as the deadline for firms to employ the "best practicable technology" for water pollution control. By July 1, 1983, new standards must be met on the basis of "best available technology." "Best practicable" was defined as a level of control already achieved by the least-polluting plants in any given
industry while "best available" went one step further. If only one plant in a given industry has a highly advanced waste control system, then that becomes the best available standard for all plants in that industry. In this case, uncertainty exists regarding precisely what "best practicable" and "best available" technology means when translated in terms of further expenditures for unproductive assets.

Another problem that complicates the environmental regulation area is the risk associated with possible conflicts between standards established by the EPA and state environmental regulations. While EPA regulations were used to illustrate the potential for risk, it should be recognized that in many of the other regulatory areas businesses face the same types of risks. In other words, new legislation may set off a wave of regulations, or government agencies may establish and/or enforce regulations, or government agencies may establish and/or enforce regulations, that may necessitate additional non-productive expenditures by the business sector. Such expenditures are analogous to the individual that is operating within a carefully-planned budget who is unexpectedly faced with a $300 auto repair bill at the end of the month.

Regulation, Risk, Return, and the Debt Capacity of the Firm. The most pertinent financial implications for small business emerge when the return and risk aspects discussed above are combined. Many factors can be identified as influencing the ability of the firm to carry and service debt. However, in the final analysis all these factors seem to point to the expected future profitability of the firm and the uncertainty associated with the profits. For example, consider the case of an investment by a firm where high future profits are expected with great certainty. In this case, the debt capacity of the firm has obviously increased (i.e., the ability of the firm to carry and service debt is greater). However, this
example is far from typical since a firm usually expects to have to accept more risk in return for the potential to attain greater profits. In other words, the ultimate impact of making this investment on the debt capacity of the firm will ordinarily depend on the relative increase in risk as opposed to the potential return.

When expenditures are made to comply with regulations, the result is likely to be unusual. Rather than adding a typical asset with, for example, a high level of risk but a good potential for return, the firm is likely to be making an expenditure for an asset that has no potential for return while increasing the risk exposure of the firm. Under these conditions, the only possible result is a reduction in the debt capacity of the firm. It should be noted, however, that even with no change in risk, mandated outlays to comply with regulations reduce the debt capacity of the firm since the rate of return on such projects is negligible.

4. IMPLICATIONS FOR SMALL BUSINESS

Defining what constitutes a small business can be a matter of opinion. The corner grocery store and American Motors could both be construed to be small businesses. Thus, a small business may be a sole proprietorship, a partnership, a small closely-held corporation, or a corporation that has stock traded on one of the major stock exchanges. Irrespective of the size or the form of organization, the primary objective of the firm should be to maximize the value of the firm for its owners. Thus, for the sole proprietor the objective is to maximize profits for the owner of the business. For the publicly-held corporation, the objective is to maximize the return the shareholder receives through appreciation in the price of the stock and from dividend payments. Two decisions that are of critical importance in
attaining this objective are the investment and the financing decisions. In other words, management wants to invest in assets that (given a certain amount of risk) yield a maximum rate of return or (given a certain rate of return) minimize risk. As management is contemplating the decision to invest, a decision must also be made regarding the financial structure of the firm or the way the expenditure is to be financed. If the latter decision is made optimally, the result will be to minimize the cost of capital to the firm.

One way to avoid some of the problems discussed here relates to the investment decision. Management may decide to diversify into areas of operation that will render the firm less susceptible to government regulations such as moving away from certain types of manufacturing to avoid making some expenditures in safety and environmental areas. However, if this cannot, or has not, been done, then the financing decision takes on an added degree of importance.

Financing a small firm is similar in many ways to financing a large corporation. Both have access to funds with differing maturities. An exception is that large corporations have access to a larger variety of instruments. For purposes of simplicity, only two basic sources of funds, debt and equity, will be considered. Equity, whether for a sole proprietorship or a publicly-held corporation, represents money put into a business by the owners of the firm. Debt entails the borrowing of funds with the firm entering into a contractual agreement to pay fixed interest payments over the life of the agreement as well as the principal.

A critical element in the financial structure decision is the appropriate amount of debt to have in the firm's financial structure. Among the more important determinants of this decision are the growth rate and stability of future sales and earnings, the competitive structure of the
industry, the asset structure of the firm, the question of owner's control, the attitude toward risk of owners and management, and the attitudes of lenders.

The term for the use of debt as a source of funds is "financial leverage." Financial leverage involves the use of funds obtained at fixed rates. Since the cost of these funds does not change when the firm's operating income varies, financial leverage can be used to improve the return to the owners of the firm. Leverage is favorable when the firm earns more on the assets purchased with fixed-rate funds than those funds cost. Conversely, leverage is unfavorable when the firm earns less on the assets purchased with the funds than the funds cost. For example, if a firm finances the purchase of an asset returning 12% with debt having a cost of 8%, financial leverage is positive. As a result, the firm earns a larger return on the owners' investment than if it had financed the new asset through equity.

While there are positive elements potentially associated with the use of debt, a high degree of financial leverage is also accompanied by a large amount of risk. The use of debt in the financial structure commits the firm to fixed charges (interest payments and principal) regardless of business conditions. Since creditors have a priority claim on both cash payments and assets, financial leverage increases the probability that the firm's owners will be unable to recover their investment in the event of adverse conditions.

Before translating this discussion into terms of government regulation, recall that the objective of management is to maximize the value of the firm for its owners. Consistent with this objective is management's attempt to minimize the adverse financial effects that are likely to occur as a result
of government regulations. It should also be noted that, as discussed earlier, it is likely that the debt capacity of the firm will be reduced as a result of government regulations prior to any decision regarding how such expenditures are to be financed. In other words, the debt capacity of the firm is likely to be reduced irrespective of the actual source of financing. Under these conditions, if the decision is made to use debt as a source of financing such expenditures, the only possible result will be unfavorable financial leverage. Although the cost of debt may be lower than for funds that do not increase fixed charges, a very careful analysis should precede the decision. This analysis should be made in terms of the revised debt capacity, that is, comparing any savings associated with the use of debt against the additional risks. The risk associated with the use of debt relates to the chance of adverse events resulting from the commitment to make cash payments that are certain in timing and amount, under uncertain future circumstances resulting from legislative risk.

An additional consideration to be made in financing expenditures to comply with government regulations relates to the idea of matching the life of an asset to the maturity of the financing. For example, an individual would obviously be unwise to finance the purchase of a compact automobile (which might have an expected useful life of five years) with a bank loan having a maturity of ten years. Likewise, other things equal, it would be financially unsound to utilize debt with a maturity of twenty years to finance equipment to comply with regulations that is likely to have a useful life of only five years due to legislative risk.

5. IMPLICATIONS FOR GOVERNMENT POLICYMAKERS

Just as management should recognize that the firm might be socially responsible, government policymakers should recognize the societal importance
of preserving the financial integrity of otherwise viable firms. Attaining
the latter is consistent with the objective of the firm as well as the
aggregate economic goals of full employment, growth, price stability, and
an acceptable balance of payments position.

Government policymakers at various levels are charged with
interpreting and implementing existing legislation as well as establishing
new legislation and/or regulations. To perform these tasks effectively,
policymakers must first understand the financial impact of regulation-induced
expenditures and, of equal importance, recognize this impact in the process
of establishing legislation and enforcing the regulations. For example,
one way to minimize the financial impact of regulations is through changes
in the tax laws.

Policymakers should further recognize that from their perspective,
the firm is complying with, for example, either an EPA regulation or an
OSHA regulation. But from the perspective of the firm, these regulations
must be complied with in the aggregate. Thus, any analysis of the impact
of one regulation without consideration of other regulations is likely to
be a short-sighted approach.

A more specific recommendation relates to economic impact statements.
Such statements have been required in the past when regulations have been
proposed and moves are underway to make these studies more meaningful.
To achieve objectives of the current movement, these economic impact
statements should go beyond their historical perspective. In the future,
they should also concentrate on issues such as inflation, productivity,
capital formation, and innovation by the business sector. In addition,
they should focus on the financial impact of regulations in terms of return,
risk, and the debt capacity of the firm. Finally, wherever the potential
exists, the economic impact statements should take into consideration the possibility of conflicts between federal and state regulations.
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STATE AND LOCAL GOVERNMENT PRACTICES
THAT AFFECT SMALL BUSINESS

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SUMMARY

Relatively little attention has been paid to steps that can be taken at state and local levels to facilitate either the growth and profitability of existing small businesses or the establishment of new small business firms. Yet such companies have always accounted for a substantial portion of the new jobs created. In recent years they have been responsible for an increasing percentage of new jobs.

Along with the attention properly given to federal laws and regulations that hamper small business growth, attention needs to be given to state and local statutes and practices that also affect small business negatively. Perhaps even more important to the survival and economic health of many small companies are the inactions of local and state government that likely have a critical effect.

The latter -- local and state "sins of omission" -- in particular offer excellent opportunities to facilitate the growth of small business firms. Unlike federal laws and regulations, actions that local governments, in particular, can take often offer short-term potentials for preventing small business failure and stimulating small business growth. Since so many small companies fail in their early years -- 80% within 10 years -- such opportunities for preventive action can be highly productive.

Among the specific steps that can be taken are providing management
and technical assistance in critical problem areas, preventing many inevitable
failures by advising would-be entrepreneurs not to go into poorly planned
ventures, teaching both established and would-be small firm owners the key
skills required for successful small business management, strengthening
small business financing programs, and filling in or correcting the many
voids and weaknesses in local government facilities and services.

1. INTRODUCTION

So much attention has been focused on the massive obstacles which
federal laws, regulations, procedures, and practices pose for small business
that relatively little attention has been paid to serious obstacles to small
business growth that can be overcome at local and state levels. This paper
focuses on the many things that can be accomplished at the local and state
levels that can have a significant effect on the success or failure of small
business -- irrespective, oftentimes, of what happens at other levels and
in other areas.

Narrowing the focus still further, attention will be given in
particular not to state laws and local statutes that may inhibit small business,
but rather to two sides of a usually overlooked coin: 1) things that can be
done by state and local governments and 2) development groups to stimulate
small business development, and things that generally are not done --
"sins of omission," if you will -- that in many cases can readily be undertaken
and can have an important effect not only on the rate of survival but also
on profitability and growth of small business firms of all types.

During more than 20 years of experience in economic development, I
have become increasingly aware that small businesses suffer often, and
unnecessarily, in ways that frequently put them out of business because no
one seems aware of their needs or does anything about them -- even though,
in many cases, the people, skills and resources required to help solve the small businessman's problems are readily available.

Rather than focus on legal and other frequently written about problems affecting the small firm, therefore, this paper centers on a real world of trouble — and often life or death — for the small business: the things state and local development agencies, local officials, and business leaders can change that can materially affect the success and failure rates of small business firms.

An important consideration is that, unlike many of the legal and especially federally imposed regulations that plague small business, the problems and practical solutions presented can frequently be worked out fairly quickly. They don't require the years usually necessary to remove legal problems, for example. Nor are they as formidable as bureaucratic policies and practices that often seem as immovable as the proverbial mountain, or as slow-moving as a massive glacier.

Wherever possible, specific cases or examples are used to illustrate problems and suggested solutions, in an effort to provide practical tools and techniques that can be put to work in any area where decision makers choose to apply them.

2. THE IMPORTANCE OF THINGS NOT DONE

Much attention has been paid to actions taken — especially in the form of laws and regulations that hamper and hamstring small business. However, things not done at state and local levels often create critical problems for small firms. Such "sins of omission" perhaps are even more costly than federal regulations. Since they haven't been studied systematically, there is no way of knowing how much impact they have — but enough examples continue to surface to indicate it has to be significant. The small
businessman may not think about or complain about such problems when surveyed, because he tends to take such omissions for granted and doesn't think of them as being correctable, as he does laws and regulations.

The single most important cause of small business failures is probably lack of adequate planning before a new business is launched. Such lack of planning is a natural result of not having information or skills needed to successfully manage a small business.

These points are, in a way, so obvious they tend to be overlooked when analyses are made of small business failures. When specific factors like "inadequate sales" and "competitive weakness" are cited as major reasons for failures, the analyst is really citing symptoms of a fundamental problem that in many cases can be effectively addressed at both state and local levels. Inadequate sales or competitive weaknesses are results, not causes.

One of the best ways to reduce small business failures is to prevent many poorly planned small business ventures from ever being established. It is likely that most of the small businesses that fail should never have been started in the first place -- at least not at the time or in the place or under the circumstances under which they were launched.

A careful review of the factors involved would have shown in advance that the new business could not be competitive, or that the market in the area was too small, or that the business person wanting to set it up lacked knowledge of the financial side of business management or that any one of a number of other fatal flaws existed in the entrepreneur's plans and abilities.

One of the most useful things my own organization does as a state development agency is to carefully review would-be entrepreneurs' plans, point out any critical flaws -- and often specifically urge the small
business aspirant not to proceed with his plans. Where appropriate, he may be encouraged to modify his plans, shift to another product or type of business, secure more capital, or work through our six week course in entrepreneurship before launching the planned venture.

Such preventive measures can be taken by state and local agencies so as not just to prevent inevitable failures but in many cases, to steer the ambitious person in a new direction that can be successful. Even where a state-level program exists like the one in Mississippi, where 25 full-time people work on new business development, expansion and diversification of established businesses, and management and technical problems, steps can be taken by local development organizations, chambers of commerce, bankers and others to organize a pre-start-up counseling program that can prevent many failures and help launch many successful business ventures.

A major omission from most state and local development programs is an information center to which business people and would-be small businessmen can come for the information they need. Such a center would have facts on sources of funding, names, locations and services of federal, state and local agencies that can provide different types of assistance, and copies of printed materials from the Small Business Administration, state and local business financing agency information, and similar material.

Local Government Problems That Hurt Small Business

Much can be done at the local level that is not now being done to prevent failures in the short run as well as to stimulate growth. Among the difficulties usually found are (1) inadequate management and planning, which produce (2) inadequate services and facilities and (3) poor zoning and land use practices, as well as (4) what is usually called "politics," and (5) indifference to the needs not just of small business but of all established
companies operating in the local area.

A typical example of the way lack of planning can be a problem that can make or break a small company -- or drive it away -- involves a local water system. A small manufacturer who wanted to add 10,000 square feet to his building found that the water pressure in his section of the city was too low to allow for the sprinkling of the planned addition. Since he could not afford the cost of the increased insurance premiums he would have had to pay if he did not have a sprinkler system, he had no choice but to ask local officials to remedy a water system problem they should have handled in their regular planning program. When local officials repeatedly refused his request to install an eight-inch looped water line to replace the six-inch dead end line that was in existence, he made plans to move his entire operation to another state where he could get what was needed. Fortunately, one of my staff members learned about his plight and was able to persuade local officials it was a legitimate request and they acted in time to enable the company to expand where it was.

Sensible zoning has been considered protection for residential use for so long that we often overlook how greatly business and industry need it for protection and healthy growth. The practical nature of this problem -- which can exist within a city as well as on its fringes, where it is most often encountered -- was illustrated by a manufacturing executive who described the difficulties he has because his city won't deal with its zoning problems.

In his case, no buffer zone was established around the manufacturing plant he operates. Over the years, as the community grew, both a shopping center and housing subdivision were built nearby. As they expanded and built adjacent to his manufacturing site, complaints started to come from shoppers and home owners about the noise and street traffic problems created by the trucks he operates in and out of his plant. He now faces constant harrassment
and expense as the result of the city's failure to zone the area around his plant for a use that would have been compatible with his manufacturing operation.

Since small companies normally have capital limitations that prevent them from acquiring their own buffer zones, as larger corporations may do, it is essential that local officials fill gaps in their city and county management and planning programs by protecting both their local government's and the company's financial interests.

In one of the cities with a top reputation throughout the South for encouraging business and industrial growth, a small manufacturing company encountered serious difficulties because it could not get city officials to understand its need for additional acreage -- land the city happened to own. The company was ready to consider moving, although it had no desire to do so, when city council members finally were persuaded to see the need and sell the property next to the company plant at a reasonable price.

Local political problems that can kill small business cover a wide range. They often seem so personal and petty they are scarcely believable -- yet they are very real and often critical to the very survival of companies we deal with. One of the most common type involves conflicts between city and county officials. Another consists of splits within local government bodies. Still another involves conflicts between businessmen who see things one way and local officials who see things quite differently.

While there is no way of knowing the total effect of such "politics" on small business, we have seen enough problems over the years to believe it to be a factor worth noting.

An example is a misunderstanding and jealousy that existed between county and city officials. An access road essential to the very survival of a number of small business firms in a shopping center was almost killed
because county officials felt the road would simply benefit city residents. Only after lengthy discussion, through which they were finally able to see the benefits to the county as well as the city, did they agree to commit the bond monies required for the construction. If they had not done so, at least a dozen small companies would have gone out of business. They simply would have been unable to compete with shops in a nearby community, which would have been more readily accessible to a sizeable residential area that was given direct access to the shopping center by the new road.

More difficult -- if not impossible -- to deal with are the sharp conflicts that sometimes develop between local officials, or between officials and local businessmen. In one instance, city officials actually rezoned to residential land around two small manufacturing plants owned by a man who had offended two city council members with his bluntness. As a result, he was prevented from expanding when he could have created several hundred additional jobs. When the manufacturer tried in desperation to get a zoning variance -- which had been granted to others -- he was refused that final opportunity to expand. As a result, employment in his two firms has dropped from about 600 to only 290. And he may eventually be forced out of business.

Needs of Existing Businesses

Local governments frequently refuse to consider local small business firms as possible recipients of ad valorem tax exemptions they readily give to new manufacturing plants -- especially branch plants of "blue chip" companies. The attitude seems to be one of feeling that someone already in the community and operating successfully should be on his own. The potential advantage to the local area usually seems to be ignored. One small company that thrives as a result of such help can pay a lot of taxes as it grows.
What appears to be an overly conservative attitude on the part of both state and local financing agencies is another problem for many small businessmen who seemingly should be able to secure funding from such agencies, but find they cannot.

An executive of a large corporation that had helped put up the initial funds for a state equity capital corporation complained recently that while his firm's investment in the state operation was a good one in the sense that it was producing a good return on their investment, he felt it was not fulfilling its purpose at all. In fact, he said, the decision makers were being as conservative in their decisions as any local banker might be expected to be with his own money -- and therefore were not providing the risk capital the program was intended to provide.

The failure of local school, city and county officials to concern themselves with the manpower needs of small business results in a great deal of frustration, increased costs, and reduced growth or even critical financial problems. In many areas -- and indeed across entire states -- industrial vocational training is concentrated in skill areas that are of no relevance or help to local small manufacturers, in particular. Most of the training is in the services -- cosmetology, auto body repair, electric installation, etc.

To be specific, analysis of one state program that is probably more typical than not revealed that of well over 100,000 people being trained in various vocational subjects, less than 12 percent, were being trained in a skill area that could possibly be of interest to a manufacturer. Small companies all across the state shared the need of many larger companies for trainees. In many counties not a single person was being trained in any skill area that might fit them to work in the manufacturing companies, large and small, that were seeking trainees. The apparent problem, which appears
to be nationwide, is that vo-tech programs tend to follow available funds -- which often are not geared to current and future skill needs.

In one local situation, a survey of local businessmen and manufacturers disclosed that they found it impossible to get acceptable trainees from the local junior college vo-tech program. Investigation revealed that there was absolutely no communication between school officials, city and county officials, and business and industry in the area.

When a committee representing companies and school administrators was set up to try to solve the problem, communications soon broke off. School officials said they had decided they should continue to set the curriculum as they had been, without outside interference. So they went back to training students in traditional skill areas, with no regard for the needs of potential employers.

Another small business need that is rarely filled at either state or local level is for information about people with special skills that are often difficult to find, particularly in smaller cities. If local school officials or development agencies can maintain a data bank of former residents who would like to come back to live if suitable employment can be found, many such manpower needs might well be met at very low cost. Such a project could be started on a limited basis simply by surveying interested local citizens through civic clubs to identify friends and relatives who want to return.

Another omission that for the most part needs to be filled at the state level involves providing a wide range of information services. However, basic reference materials need to be located within 50 miles of a small business if they are to be useful, so it is important for state agencies to disseminate their information through regional centers wherever possible. This can likely be done through existing facilities at colleges and public...
libraries and would not require new government installations.

In addition to basic reference materials, technical books, and films, it helps small businessmen to have ready access to such information as compilations of major government regulations affecting small retail businesses in a state, or a checklist of state legal and regulatory requirements that must be met by manufacturers. Directories, periodicals of special types, maps, and such special data as Census printouts are essential to adequate planning.

3. THE ECONOMIC VALUE OF SMALL BUSINESS

Before considering some of the practical steps that can be taken at state and local levels to encourage the development of small business, let's take a quick look at the question of what it's worth. How much do small businesses contribute to economic growth?

On the average, over a period of many years, half the new jobs added to the economies of most states have come from expansion of existing companies of all types. Most of these are small. And since small businesses employ 55% of all private sector, non-agricultural workers, it seems reasonable to assume that at least a third to one half of the new jobs added to the economies of most states result from the expansion or establishment of small business firms.

The trend in recent years -- almost certain to continue for the indefinite future -- has been for corporate branch plant locations to slow. Inflation, high interest rates, and uncertainties about federal policies tend to increase the importance of economic growth from expansions and new business development. Between 1977 and 1978, for example, almost 63% of Mississippi's manufacturing job gain came from expansions and the establishment of new ventures -- up substantially from what it has been.

Is it worth it to a state or local government to spend some of its
tax revenues on programs aimed at stimulating the development of small business? It certainly is. But few states have made more than a token effort to date. The Economic Development Administration's "University Center" program, for example, in most states has produced a staff of only three to five people devoted to helping small companies with their growth and survival problems. The matching funds required from the participating state agency -- usually a university -- generally falls in the $50,000 to $75,000 category. That's not much of an effort in support of such a significant part of a state's economy.

Another pertinent question that needs to be answered by state and local governments as they consider the question of whether to spend money to help develop small business is the broad question of how they should spend their tax revenues overall. This moves quickly into the "meddling" area, since the answer requires that legislators and county and city officials analyze their allocations and consider changes that may be needed to facilitate economic growth.

An important fact often overlooked is that general fund revenues are one of a state's primary economic development resources. For the most part, only superficial attention is paid by either state or local governments to one of the most important questions that can be asked by any elected official: How can tax revenues best be allocated to stimulate healthy economic growth?

As soon as this question is asked, problems are likely to arise with established agencies and bureaucracies that are obsolete and obsolescent. But with revenues limited and both national and international economic situations that are unique in our history, with the future relatively unpredictable as a result of the energy situation and the unprecedented flow of capital to the Mideast, it seems highly relevant to ask such questions.

To cite only one possible application, agriculture at present contributes
only about 5% of Mississippi's income, yet the sums allocated for agricultural research and extension are many times the totals available for development of all other sectors of the economy. The same situation exists in many other states.

Another interesting question for both state and local governments to consider is this: What would happen to their economic growth if they put as much money, time and effort into stimulating the growth of small companies already in business within their borders as they do in trying to attract new companies from outside their area?

Since the chances of attracting one of the relatively small number of new manufacturing plants established each year to a particular location are relatively small, it might reasonably be argued that it makes more sense to put effort and money into a program aimed at expanding existing businesses. This is likely to become even more the case in the years immediately ahead, for the reasons cited above.

All factors considered, it appears as though dollars invested in an effective effort to expand companies already located in an area could be expected to produce a much higher return than dollars spent trying to attract one of the increasingly scarce new manufacturing plants or other new business operations to be located in any 12-month period somewhere in one of the 50 states.

4. SOME STATE AND LOCAL GOVERNMENT OPTIONS

What are some of the options that state and local governments might consider, if they decide to address in a businesslike and systematic manner the question of how best to stimulate the establishment of new businesses and the expansion and diversification of companies already doing business in their areas?
One of the most obvious considerations is one that has been much written about and therefore will be touched on only lightly here: the establishment of one or more types of financing agencies. Most states and many cities across the nation already have appropriate corporate entities in operation, from state equity capital and minority funding entities to local development corporations.

Perhaps two points need reiteration: First, many existing financial institutions are under financed. Second, our experience is that many are so extremely conservative in their approach that they miss many of the best opportunities to stimulate small business firms with really outstanding potential.

State Technical Services

A service that can be provided to state or local financial agencies that might well be handled by a qualified state agency is a combined technical-economic evaluation of ventures for which funds are sought. If a suitable state agency does not exist, consulting firms might profitably be employed. Where a proposed venture may be turned down because of its technical nature and complexity -- and especially where a potentially high return exists -- the relatively high cost of a consultant's evaluation may be a good investment.

Entrepreneurial Training

The training of potential and operating entrepreneurs can be an important part of a state economic development program. Everyone knows that 80% of all new business ventures fail within the first 10 years. What everyone does not know is that in many cases the failures could be prevented if the entrepreneur had only learned a skill or two that he didn't have.
Many businesses founder because of the owner's lack of understanding of the principles of financial management. One of the not too difficult things a state agency can do is develop a computerized cash flow model that can be used to quickly show a small businessman his cash flow problems and needs.

A short course or workshops that explain in practical fashion the basic skills required to successfully operate a small business is an essential part of any state development program that aims to support the establishment and growth of small business. Approximately 25 such workshops were held in Mississippi during the past 12 months in almost as many locations. Each involved six three-hour sessions, held one night a week for six weeks. Such workshops not only help launch new ventures on a sound base, but can teach people struggling to survive in established firms skills they require to keep from becoming another business failure statistic. In-depth workshops on topics like tax planning, financial management, and sales and marketing can also be extremely valuable.

New Venture (and Failure) Prevention

A frequently overlooked step that our staff takes regularly is to discourage a would-be entrepreneur from going into business in the first place, as noted earlier. Many of the early failures are 100% mistakes—that is, they should never have been undertaken at all. If the person involved has the necessary technical skills he may lack the management or sales skills. If he has those, he may be undercapitalized. If he has enough money, he may be getting into a field in which he has no chance to compete successfully, or for which there just isn't a large enough market in the area he wants to serve. Although difficult, the best thing in the world to tell many people who want to go into business is "Don't!" Normally, they
will be extremely appreciative after they have recovered from the initial shock and have time to get their situation in perspective. Often, they can be encouraged to go into another type of venture either in the short run or at a later time -- one that has a reasonable chance of success.

**State-Level Expertise**

Initiative needs to be taken at the state level in most instances to establish practical, problem-solving management and technical assistance programs. However, in larger cities it should be possible to fund staffs of sufficient size and skills to carry out a comprehensive program at the local level.

State level programs exist in about half the 50 states now, although for the most part they are quite small and can handle only a fraction of the work that needs to be done. An example of the magnitude of the task even in a small state like Mississippi can be seen in the constant backlog of requests for assistance that faces the staff of 25 full-time persons working in this area.

An addition to the Mississippi program during the fiscal year just started will no doubt increase the backlog. For the first time a portion of the staff's time will be allocated to seeking out healthy companies that are good candidates for expansion but are not requesting help, as opposed to our traditional pattern of simply responding to requests for assistance. However, taking time to identify such "best bets" for growth is something we feel can pay off well in new jobs for the state. In many cases, this likely will mean identifying growth opportunities -- either through expansion of an ongoing operation or adding a new product or products -- that local management, for various reasons, hasn't identified. From a practical point of view, the manager of a small business frequently is so busy fighting his day-to-day
battles he simply doesn't have time to sit back and gain the perspective required to see growth opportunities. Since such opportunities may not only be important to his profitability but even to his survival, a state small-business development program can make an important contribution in this area.

Local Talent

It may be possible in many instances to identify retired local businessmen who can make valuable contributions to such a program. The SBA's "SCORE" program may be of help. Or an informal project can be set up to use available management and technical skills. A great deal of expertise and energy go to waste each year in any community of any size in the form of unused skills. Often the persons with the skills are not only willing but eager to be of service when asked.

Local Services

What can be done at the local level, particularly in a relatively small community, to fill the needs of small business? How can a local development group or chamber of commerce possibly do much, with the limited staff and funds they usually have?

Much can be accomplished by providing a liaison and information service. For example, a local group can keep an up-to-date list of agencies than can be of assistance -- such as a state development agency that works with existing companies. It can see that all small businesses in its area know about such agencies and the services they can provide.

Perhaps as important, it can budget at least a limited amount of time to call on a few firms each month to learn whether there are problems that the local development group might help resolve. In some instances this may require calling city or county officials' attention to a problem only they can
solve. Communication from the agency's board of directors to local officials may be needed to ensure that such problems receive proper attention. Lack of such action and support from a chamber of commerce or other local development group can mean a company has an uphill fight to get what it needs and often is entitled to in the way of local government facilities and services.

To supplement the computerized data bank a state development agency may maintain, such as the one we have compiled of university graduates who would like to return to Mississippi, local organizations can set up a file of information of the sort mentioned earlier on former residents with special skills and experience who would like to return to their home areas. Such a data bank can be started simply by asking the directors of the local development group to list people they know, and then have friends, business associates and relatives do the same thing. Without a great deal of cost or effort on anyone's part, a substantial list of skilled people can be developed who might be just the persons needed to help fill a manpower need of a local small company.

This can be particularly important to small businesses, because they obviously can't afford to advertise or seek widely for people they need. In some instances, it may be possible to arrange for a former resident to provide a part-time service to several small firms, thus ensuring an adequate level of living where it would otherwise not be possible for a single small company to afford the expense -- of a cost accountant or an industrial engineer, for example.

Technical Training

Local officials can take the initiative in another area where deterrents are likely to exist for businesses and industries of all sizes -- the provision of technical training in high schools and junior colleges. An example has
already been given of the types of problems that frequently arise.

In ways that are especially important to the businessman, our schools for the most part are completely out of control. In general, accountability in the field of education seems to mean simply providing figures that indicate how an educational system's money was spent, with little or no reference to results secured -- the return on the investment made. Like some of the uncertified audits used by some city and county governments, such reports tell very little, except that the arithmetic represented in the accounting was done correctly. Key questions usually remain unanswered, such as what the organization's goals were, whether those goals made sense, whether the learning needs of children in the system were met, whether additional things need to be done to meet the learning needs of the unusually bright students, in particular -- in short, whether the taxpayers are getting their money's worth.

It is perhaps worth noting that in Mississippi, approximately 63% of general fund revenues goes for support of public schools. In the larger cities in the state, school budgets are about the same size as the total spent for all other expenditures combined.

The reason for calling attention to this point is that the business community, large and small, is heavily dependent on the people supplied to it through the public school system. If -- as often seems to be the case -- high school graduates can't pass the equivalent of fifth grade reading and math tests, the company that hires such people has a big problem.

Perhaps even more important, the "social promotion" policy that seems to exist on a wide scale tends to inculcate a non-work attitude that militates against those who go through the system ever becoming productive employees. A small business can go broke before it can find the time to
reshape the mental habits and work attitudes of individuals who enter the work force from such an educational system.

It therefore makes sense for both state and local development groups and officials to talk to representative companies, small and large, to learn whether they can find in the local area the kind of employees they need. At the same time, it makes sense to check on the types of training being provided in technical and vocational programs. At the very least, a permanent communications system should be set up to provide for regular discussions between curriculum planners and the firms that are the most likely employers of those who will be going through the school programs.

This is not to say the business community should control programs and practices. But it is important to make sure that the large sums being spent for such programs are first, being spent for relevant courses of instruction, and second, that the instructors have sufficient familiarity with the real world of work to be able to teach the right skills and attitudes.

5. CONCLUSION

With all the obvious problems created for small business as a result of federal laws and regulations, as well as state laws that hamper small business development and operation, it is easy to overlook the fact that much can be done at the state and local levels to enhance small business development.

A major problem affecting a high proportion of small businesses is that their needs are simply ignored by officials and development agencies alike. In many instances a great deal could be done to prevent failures and to stimulate growth by actions that are relatively easy and inexpensive.

Management and technical services that may require professional staff and substantial expenditures need to be an integral part of every state's economic development program, however, because of the large and
increasing contribution to economic development being made by small business. Because of extraordinary national and international economic conditions, investment in programs aimed at helping established companies expand and increasing the number of successful small businesses established likely will pay a considerably higher dividend than programs aimed at attracting new payrolls from outside a state or local area. Both, of course, are needed to maximize any area's growth.

Eliminating the "sins of omission" that presently are normal to local and state governments can do a great deal to prevent the demise of many small businesses, as well as to stimulate small business growth and new business development.
1. INTRODUCTION

In recent years, the number of laws affecting business at all levels has grown tremendously in the American economy. The Occupational Safety and Health Administration regulates safety in the workplace; the Consumer Products Safety Commission regulates safety of products; the Employee Retirement Income Security Act governs pension plans; and several federal regulatory agencies and laws are concerned with non-discrimination on the basis of age, sex, and race. These laws are all aimed at supplementing market forces in various ways. They have important effects on both large and small businesses. (For a good discussion of the nature of the laws and some of their effects, see Weidenbaum, 1977.)

In this paper we will be concerned primarily with the sources of the legislation. That is, we will examine the forces which are involved in passage of such laws. The method used will be a statistical examination of the forces associated with voting by Congressmen for passage of laws which have impacts on small businesses. We have used this method of analysis elsewhere (Kau and Rubin, 1978, 1979a, b) and have found that it is very useful for explaining the passage of various types of legislation.

One determinant of legislation is the campaign contributions of various interest groups. As we have shown elsewhere, such campaign contributions have important impacts on the passage of legislation. Moreover, Congressmen
who vote as contributors desire are likely to receive contributions from interest groups. A rational strategy for contributors is to give money to those Congressmen who are likely to vote as the contributor desires. Thus, one part of the paper will examine the contributions of various donors to election campaigns, including business contributors.

In Section 2 of the paper, we will examine the economics of regulatory legislation, with particular emphasis on OSHA as an example. We will argue that the passage of such legislation is based on a fundamental misunderstanding of the nature of market forces. Moreover, we will discuss the relative impact of regulatory legislation on small and large business. In Section 3 we will examine voting by Congress on twenty-two bills which have important impacts on small business and identify some of the forces which are involved in such voting. In Section 4 we will examine the determinants of campaign contributions by various interest groups, including business contributors. In both sections 3 and 4 we will include variables which will enable us to determine the differential impacts on legislation of regional variables as well as the general variable considered.

2. THE SIMPLE ECONOMICS OF REGULATION

As discussed above, we are reaching a situation in which more and more aspects of business behavior are regulated by specific agencies of the Federal Government. It is not clear why this regulation is occurring and why the amount of regulation has increased so dramatically in recent years. The economic theory of regulation (advanced by George Stigler, 1971, and modified and extended by Sam Peltzman, 1976) argues that most legislation is passed to benefit special interests groups. This theory can easily explain the "old" regulation. Economists have little doubt, for example, that the main effect
of the Interstate Commerce Commission is to benefit truckers and railroads at
the expense of shippers. However, these theories do a worse job of explaining
the new wave of regulation; it is not clear which interest groups benefit from
OSHA or from the CPSC.

We have elsewhere generated information which indicates that ideological
factors are at least in part responsible for the passage of much legislation.
(We will re-examine this hypothesis in this paper as well.) In the case of
regulation affecting business, part of the reason seems to be a profound
anti-market sentiment among some powerful segments of the population. Part of
this hostility may be based on dislike of the methods and results of economic
competition. However, some of the increased regulation may also be due to a
misunderstanding of the manner in which market forces operate. In this section
we will examine the market for workplace safety and show how market forces will
operate to generate efficient amounts of safety, independent of any legal
restrictions on safety. The example chosen is somewhat arbitrary; similar
arguments could be made about many other aspects of behavior which are regulated
by statute instead of by market forces.

Consider some employer who is concerned with maximizing profits. (The
assumption of profit maximization is standard in economic theory.) Let us
make the stronger assumption -- assume that the employer is completely
indifferent to the safety of his workforce. (We do not believe this to be
ture, but our results hold even if it is true; that is, the desires of the
employer may be irrelevant for determining the amount of safety.) Will such
an employer have any incentive to invest in safety on the job?

The answer is, of course, yes. Market forces will require him to invest
in safety; moreover, these market forces will force him to invest in the
optimal amount of safety as measured by the desires of workers for safety.
The mechanism is simple: workers do not like unsafe jobs. This means that workers will require higher pay to work in a job which is unsafe. An employer then has two choices: he can invest in safety equipment or he can pay his workers premiums based on the degree of risk on the job. If the employer is economically rational and concerned only with his own profits, he will attempt to minimize the cost of accidents. This cost is made up of two components. One is the premium which he must pay workers for bearing risk; the other is the expenditure on safety equipment. The rational employer will invest in safety to the point where the last dollar spent on safety equipment will be just as productive as the last dollar paid in additional wages to workers to induce them to bear risks. Notice carefully that the workers themselves decide how much they are willing to pay for safety. If, for some reason, workers decide that they want more safety, then the premium which they demand for unsafe working conditions will increase. Historically, in the United States, as worker incomes and education have increased, workplace safety has also increased as shown by Chelius (1977.) Presumably, what has happened is that workers have been demanding higher premiums for bearing risk and as a result employers have found it worthwhile to invest in additional workplace safety.

The above argument depends on two assumptions. First, we assume that workers can perceive the risks in various jobs. Second, we assume that workers do not like risky jobs. In the case of safety, both of these arguments seem warranted. (Health may involve different issues; we will discuss this below.) For example, Thaler and Rosen (1976) have deducted evidence which indicates that workers demand premiums for risky jobs. Requiring of such premiums indicates that in fact workers know that some jobs are riskier than others. Thus, in the case of risk, evidence indicates that workers do actually perceive
that some jobs are riskier than others.

If this is so, how can we justify legislative intervention into workplace safety? The argument must be paternalistic -- that is, there must be some argument which says that workers do not choose enough safety. We, the government, must know more about the optimal preferences than workers know themselves. Economists are generally skeptical of paternalistic arguments; it seems unlikely that some arm of the government will know more about my preferences for risk (or anything else) than I know myself. Moreover, it is somewhat peculiar to think that workers underestimate the probabilities or costs of risks but that voters (who are after all also workers) can more correctly perceive these costs.

It may be possible to argue that workers do not correctly perceive the dangers of certain occupations. While this is probably not true for accidents, as discussed above, it may be that workers do not perceive risks to health from certain activities. Of course, in some cases, no one knows about health risks; in these circumstances, the government can do no better than workers. However, it might be efficient for the government to sponsor research into the health implications of various occupations, since it can be argued that markets will not provide efficient amounts of information. Even if we accept this, however, it is not a reason to regulate safety; rather, it is an argument for making additional information available to workers, who could then choose their own desired level of safety based on the new information.

Moreover, Viscusi (1979) indicates that OSHA has actually spent very small amounts on health inspection, and fewer than 1% of all violations have been health related.

Thus, from whatever perspective we examine OSHA, it is clear that it is economically inefficient. Similar arguments apply to most of the areas
currently regulated by government. If products are unsafe, consumers will pay less for them; if they are too unsafe, legal action against manufacturers might result. Thus, there is little reason to legislatively intervene and require additional safety for products. Similar arguments could again be marshalled about most government regulation. Finally, Viscusi (1979) shows no effect of OSHA on safety.

Moreover, it is likely that much of the recent regulation has had disproportionate effects on small business. One of the major implications of the new regulation is a requirement of substantial increases in record keeping by firms. This increase in record keeping is somewhat in the nature of a fixed cost, independent of the size of the firm. To the extent that this is so, the burden on small firms would be proportionately larger than the burden on large firms. Thus, we may say that the recent wave of government regulation is economically inefficient -- incomes of consumers and of firms are lowered by this regulation. Moreover, a large share of this cost is borne by small business.

3. SOURCES OF LAWS

If these laws are inefficient as described above, a natural question to ask is, why have they been passed? Economists know something about the political process as it effects laws which have economic impacts. The theory proposed by George Stigler (1971) and modified by Sam Peltzman (1976) and others indicates that in general interest groups with concentrated interests will be able to influence the legislature and obtain passage of laws which have favorable impacts on the members of the group. The theory holds that this may occur even in situations where the gains to those who benefit from the legislation are less than the losses to those who lose (the economic
definition of inefficiency) since in many cases the gainers are more politically aware of the effects of laws on their own situation, while the loosers may be very diffuse. But more recent types of regulation provide a puzzle for this theory, since we are unable to identify the interest groups which benefit from many of the laws which have been passed.

In an attempt to solve this problem, we have done research on determinants of voting by Congress (Kau and Rubin, 1978, 1979a, b). Our working hypothesis has been that, whatever the ultimate sources of laws may be, it is nonetheless true that ultimately all national laws must be passed by Congress. Since this is so, a possible way to examine the source of legislation is to look at the factors which lead a Congressman to vote for or against some bill. In this way, it may be possible to identify various groups which favor or oppose particular laws and thus to determine sources for the legislation.

**Independent Variables**

In our choice of independent variables, we have attempted to control for most economic and sociological variables which might affect the way in which a Congressman votes. The variables used have been:

- **Central City**: the percentage of voters in the district who live in a central city area.
- **Education**: the average education of the voters in the district. Education is highly correlated with income, so we are unable to use both education and income in the same analysis. Previous research has indicated that the use of education itself does not bias the results.
- **DOD, HEW**: we use spending by the Department of Defense and by the Department of Health, Education, and Welfare in the district. These variables are included to determine if spending in the district by government
agencies has impacts on the voting by the Congressman. Most government spending is by these two agencies. However, in other research we have included total government spending is analyzing some votes; the results are not significantly modified.

Farm: we use the percentage of residents who are farmers as one variable. This should be especially important in votes which have urban-rural differences in impact.

Black: we use the percentage of blacks in the district. This would be expected to be significant in explaining voting on bills with a Civil Rights emphasis and, because of the historic position of blacks in the American economy, we would also expect number of blacks to be important in explaining voting on bills which have impacts of the poor.

Union Membership: Since unions are important political as well as economic institutions, we would expect the number of union members in a district to be important in explaining voting. Unfortunately, we have been unable to obtain data by Congressional district on union membership. Thus, this variable is measured on a statewide basis. This may serve to bias the coefficients of this term downward. (The data source for union membership by state is Handbook of Labor Statistics.)

Nixon: This is a variable defined as the percentage of voters in the district who voted for Nixon in the Nixon-McGovern election of 1972. We use this variable as a measure of ideology, since we feel that our other variables have controlled for economic interests of constituents. In other research, we have used the ADA (Americans for Democratic Action) rating earned by the Congressman as a measure of ideology. However, ADA ratings and Nixon voting are correlated with an $R^2$ of -.69; thus, either of these variables is probably a good measure of ideology. Nixon voting is probably somewhat preferable
since it is a direct measure of constituent ideology. (We sometimes refer to Nixon voters favoring some bill; we could in all cases equally well have referred to McGovern voter as opposing the bill.)

Seniority: We use a measure of the seniority of the Congressman in order to determine whether more senior Congressmen behave differently from others.

Margin: We also control for the percentage of votes which the Congressman received in the most recent election.

North-South dummy: We use a dummy variable which takes on the value of 1 for Congressmen from Mississippi, Alabama, Florida, Tennessee, Kentucky, North Carolina, South Carolina, and Georgia, the states in Federal Region IV, and 0 elsewhere. Part of the purpose of the research is to determine the differential impact of laws within the region, and we wanted to determine if Congressmen from the region were subject to different influences than Congressmen from outside the region.

In addition to constituent characteristics, we also used measures of campaign contributions received by the Congressmen from various interest groups. The groups which we have used are:

Business Contributions: These are campaign contributions received from business contributors in 1972 as reported by Common Cause. Most of these contributions may be conceived as coming from Small Business. This measure of contributions is somewhat incomplete since contributions given by businessmen and executives directly would not have been counted as being business contributions in the Common Cause compilation.

Agricultural contributions: These are contributions from agricultural interests. In fact, most of the agricultural contributions were from those in the milk business.
Medical Contributions: Contributions from various health related organizations.

Union Contributions: Unions are important political as well as economic institutions. They are also significant contributions to political campaigns. The total amount of contributions from economic interest groups reported by Common Cause was $8.5 million. Of this, unions contributed $3.6 million while business contributed $1.7 million. (As mentioned above, not all business contributions are counted.) Unions also contribute services to politicians; we have no measure of the value of these contributions.

Bills Used

We have taken a sample of 22 bills from 1973 to 1974 which we felt might have had significant impacts on Small Business. (See Table 1) The bills are:

Small Business Administration (2 votes): Two bills deal with the level of appropriations for the SBA. SBA is an arm of government which makes loans to small businesses, provides managerial services for such businesses, and sponsors research on small business. This, small business might be expected to favor appropriations for SBA.

Energy (2 votes): Two votes dealt with various aspects of energy allocation. One vote would have deleted provisions which allowed retailers to agree on hours of operation in order to conserve energy without being subject to antitrust laws. Many retailers are small businesses. The second energy vote (No, 4) would have exempted owners of small oil leases from restrictions of windfall profits.

Federal Elections Campaign Act (3 votes): This law had significant effects on the possibilities of contributing to electoral campaigns and would thus serve to redistribute political power in the United States, probably away
from financial contributors such as business and toward contributors of goods and services such as unions. Vote 5 ended debate on the issue; vote 6 would have added certain restrictions to contributions; vote 7 lowered campaign ceilings for the House from $75,000 to $60,000.

Minimum Wage (3 votes): Minimum wage laws add significant impediments to the functioning of the economy since they mean that low productivity labor is often forced to become unemployed. It seems likely that small businesses are likely to hire relatively more low wage labor; we would thus expect small businesses to oppose such legislation. Bill 8 would have exempted those under 18 from the full effect of the minimum wage law; bill 9 was the final passage of the bill; bill 10 was also an attempt to exempt youths from the provisions of the minimum wage law.

Wage-Price Controls (3 votes): Wage price controls significantly impede the functioning of the economy since the informational effect of prices is severely hampered by this legislation. It is not clear whether small business would suffer more or less than large business from this legislation; but all business is adversely affected by such laws. Bill 11 extended the President's authority to control wages and prices; bill 12 would have somewhat exempted farm products from controls; bill 13 would have recommitted the controls bill to committee.

Consumer Protection Agency (3 votes): The Consumer Protection Agency would have represented "consumer" interests before other government agencies. Its major effect would probably have been to further add to decision making costs; in general, markets provide the best possible protection for consumers. Bill 14 would have limited the agency's right of judicial review; bill 15 would have limited the agency's access to other agency records; bill 16 would have limited the time of the authorization of the agency.
### Table 1: Bills Used in the Study

<table>
<thead>
<tr>
<th>Bill</th>
<th>Vote</th>
<th>Republican</th>
<th>Democrat</th>
<th>Northern Democrat</th>
<th>Southern Democrat</th>
<th>Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>17. OSHA Appropriations</td>
<td>201-194</td>
<td>132-45</td>
<td>69-149</td>
<td>14-129</td>
<td>55-20</td>
<td>June 27, 1974</td>
</tr>
<tr>
<td>18. OSHA Appropriations</td>
<td>301-100</td>
<td>169-10</td>
<td>132-90</td>
<td>65-81</td>
<td>67-9</td>
<td>June 27, 1974</td>
</tr>
<tr>
<td>20. OSHA Appropriations</td>
<td>190-182</td>
<td>126-42</td>
<td>64-140</td>
<td>14-120</td>
<td>50-20</td>
<td>June 27, 1974</td>
</tr>
</tbody>
</table>

**Note:** Congressional Quarterly Almanac
OSHA appropriations (4 votes): As discussed above in Section 2, the Occupational Safety and Health Administration basically serves no useful purpose in our economy, but merely adds substantial costs to business decision making. Moreover, we would expect these costs to fall disproportionately heavily on small business. Bill 17 would have prohibited any funds for OSHA inspectors inspecting firms with 25 or less employees; bill 18 would have earmarked some OSHA funds for consultation with employers; bill 19 would have reduced OSHA appropriations; bill 20 also dealt with inspections of small businesses.

Bill 21 dealt with consumer product warranties; it would have given the FTC additional power to seek redress for consumers injured by "unfair" trade practices. The major power of consumers is through markets; the FTC does little to help consumers, especially in this area (see Jordan and Rubin, 1979).

Bill 22 would have extended the life of the Export-Import Bank, which provides financing for businesses engaged in exporting and importing.

Results

The results of the statistical analysis are significant (3). The most prominent result—which is consistent with other research—is that ideology, as measured by voting for Nixon in the Congressmen's district, is highly significant. This variable is statistically significant in 20 of the 22 votes. Thus, on the bills affecting small business, conservative voters have important impacts. Moreover, these voters would have generally favored positions favorable to small business. The only votes in which this variable was not significant were those dealing with the SBA. It could be that conservative voters favor small business but are opposed to government intervention in general; this would explain the lack of significance of this variable on this issue.

The second important result is that union contributions were significant also on 20 of the 22 votes; moreover, union contributions always had the oppostie
sign from Nixon voting. Thus, if we take Nixon voting as a measure of conservatism in the economy and as a measure of a desire to restrict the size and power of government, it appears that unions are an important group which favors increased government intervention in the economy. Since the set of bills examined here would have had important impacts on small business, it appears that the laws favored by unions would generally serve to hinder the functioning of small business. Union membership was significant less often than union contributions, which indicates that much of the political power of unions may come from their campaign contributions. (However, as discussed above, there are problems with our measure of union membership).

The number of black voters in a Congressman's district is a significant variable in nine votes; moreover, interestingly enough, when significant this variable always has the same sign as Nixon. This indicates that blacks seem to oppose laws which increase the government presence in the economy. Since many or most of these laws have negative impacts on blacks (e.g., minimum wages lead to significant increases in black unemployment), this result is not surprising; moreover, it is consistent with results which we have obtained elsewhere (Kau and Rubin, 1978). Education is significant nine times and generally agrees with Nixon. Defense spending is significant 6 times and generally of the opposite sign from Nixon. HEW spending is significant seven times and opposite in sign from Nixon, indicating that an important component of conservatism as measured by Nixon voting is a desire to reduce the size of government. Farm population is significant eleven times and always has the same sign as Nixon voting.

Business contributions are significant seven times; we discuss this variable below. Agricultural contributions are significant five times and generally agree with Nixon voting; medical contributions are significant eight times and generally agree with Nixon voting. The north-south dummy is significant only six times, indicating that on issues effecting small business, Congressmen
from this region do not behave very differently from other Congressmen after adjusting for economic and other interest of constituents and contributors.

The main purpose of this study is to determine the effect of business contributions on voting by Congressmen on bills affecting small business. We see that business contributions were significant seven times in explaining voting by Congress. This result is somewhat surprising, since we have chosen a set of bills which would be expected to have a disproportionate impact on business and we nonetheless find that business contributions were insignificant in two thirds of the cases. Business contributions are significant in explaining voting for the SBA on both votes; they are significant in explaining voting on the campaign act twice; in explaining voting to exempt small oil wells from profit limits; and in voting against strengthening the FTC and the CPA. However, these contributions have no impact in explaining voting on OSHA or on wage-price controls, both of which are important issues. Thus, businessmen seem to use their campaign contributions to affect voting on some issues of relevance to business, but not on other issues. The political impact of unions seems to be much greater than the political impact of business.

Finally, from the levels of $R^2$ and of correctly predicted voting, it appears that we have done a reasonably good job in explaining voting by Congress, so that our results are somewhat reliable.

4. DETERMINANTS OF CONTRIBUTIONS

In the previous sections, we examined voting by Congressmen as a function of campaign contributions and constituent characteristics. However, campaign contributions are themselves functions of the way in which Congressmen vote. In this section we will examine the factors which affect contributions.(2) (Note that contributions were received in 1972 and the voting occurred in 1973-74. Thus, we assume that contributors could determine in advance the way in which Congressmen would vote. Since most Congressmen are incumbents with a past
history of voting, this is not an unreasonable assumption. Moreover, non-incumbents would attempt to notify potential contributors of their positions.

The results of our analysis are in Table 2. This table reports multiple regression analyses of determinants of contributions from each of our contributing groups (Business, Agriculture, Medical, Union) as determined by constituent characteristics, characteristics of the Congressman (seniority, electoral margin), and voting by the Congressman on ten bills. (These ten bills were chosen so that there would be one bill in each of the major areas of legislation examined.) We are particularly concerned with the determinants of business contributions, and particularly with the impact of voting by the Congressman on bills affecting business. We see that such voting is significant in only three cases; by contrast, voting by the Congressman is significant in explaining contributions from unions in six cases (both out of ten). Thus, this indicates that unions do a relatively better job of allocating their campaign contributions than does business as a function of the voting behavior of the Congressman.

5. SUMMARY

In this paper we have examined political factors which affect small business. We were interested in this topic because of the recent increase in the number of laws which have adverse impacts on business in our economy. We were concerned with trying to explain the forces behind the passage of these laws.

Our major finding is that these laws may be explained by a combination of ideology and of union campaign contributions. Thus, Congressmen from districts which are relatively liberal, as measured by the percentage of voters voting for McGovern in 1972, tend to vote for increased government control of business. Also, Congressmen who receive contributions from unions vote for such bills.
The following is a table showing the determinants of contributions.

<table>
<thead>
<tr>
<th>Determinant</th>
<th>Business</th>
<th>Agriculture</th>
<th>Medical</th>
<th>Union</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>3094.11</td>
<td>-669.192</td>
<td>326.567</td>
<td>3677.67</td>
</tr>
<tr>
<td></td>
<td>(1.253)</td>
<td>(-.382)</td>
<td>(1.298)</td>
<td>(.744)</td>
</tr>
<tr>
<td>Union</td>
<td>-4.909</td>
<td>3.092</td>
<td>.267</td>
<td>18.336</td>
</tr>
<tr>
<td></td>
<td>(-.320)</td>
<td>(.264)</td>
<td>(.017)</td>
<td>(.598)</td>
</tr>
<tr>
<td>Central City</td>
<td>11.231</td>
<td>5.685</td>
<td>4.875</td>
<td>10.923</td>
</tr>
<tr>
<td></td>
<td>(2.662)</td>
<td>(1.899)</td>
<td>(1.135)</td>
<td>(1.295)</td>
</tr>
<tr>
<td>EDU</td>
<td>146.824</td>
<td>185.131</td>
<td>112.838</td>
<td>147.378</td>
</tr>
<tr>
<td></td>
<td>(.985)</td>
<td>(1.751)</td>
<td>(.744)</td>
<td>(.494)</td>
</tr>
<tr>
<td>DOD</td>
<td>.243</td>
<td>-3.200</td>
<td>.122</td>
<td>-1.777</td>
</tr>
<tr>
<td></td>
<td>(-.618)</td>
<td>(-.717)</td>
<td>(.304)</td>
<td>(-1.494)</td>
</tr>
<tr>
<td>HNW</td>
<td>2.066</td>
<td>.365</td>
<td>-1.657</td>
<td>2.252</td>
</tr>
<tr>
<td></td>
<td>(-1.544)</td>
<td>(-.584)</td>
<td>(-1.217)</td>
<td>(-.842)</td>
</tr>
<tr>
<td>Farm</td>
<td>-24.847</td>
<td>182.651</td>
<td>13.568</td>
<td>57.511</td>
</tr>
<tr>
<td></td>
<td>(-.829)</td>
<td>(8.381)</td>
<td>(.444)</td>
<td>(.959)</td>
</tr>
<tr>
<td>Black</td>
<td>-5.724</td>
<td>1.553</td>
<td>-5.936</td>
<td>-6.307</td>
</tr>
<tr>
<td></td>
<td>(-.337)</td>
<td>(-.205)</td>
<td>(-.547)</td>
<td>(-.296)</td>
</tr>
<tr>
<td>Nixon</td>
<td>-6.007</td>
<td>-1.791</td>
<td>-16.115</td>
<td>89.614</td>
</tr>
<tr>
<td></td>
<td>(-.417)</td>
<td>(-.175)</td>
<td>(-1.089)</td>
<td>(3.107)</td>
</tr>
<tr>
<td>Seniority</td>
<td>32.281</td>
<td>-16.619</td>
<td>-40.660</td>
<td>-36.159</td>
</tr>
<tr>
<td></td>
<td>(2.349)</td>
<td>(-1.704)</td>
<td>(-2.907)</td>
<td>(-1.516)</td>
</tr>
<tr>
<td>Margin</td>
<td>-41.786</td>
<td>-23.708</td>
<td>-32.547</td>
<td>-114.499</td>
</tr>
<tr>
<td></td>
<td>(-4.746)</td>
<td>(-3.798)</td>
<td>(-1.632)</td>
<td>(-6.503)</td>
</tr>
<tr>
<td></td>
<td>(2.688)</td>
<td>(.832)</td>
<td>(1.700)</td>
<td>(-1.225)</td>
</tr>
<tr>
<td>10. Minimum Wage</td>
<td>324.779</td>
<td>-349.916</td>
<td>282.118</td>
<td>-1749.51</td>
</tr>
<tr>
<td></td>
<td>(1.074)</td>
<td>(-1.650)</td>
<td>(.916)</td>
<td>(-2.892)</td>
</tr>
<tr>
<td>11. WPC</td>
<td>39.167</td>
<td>-60.521</td>
<td>-75.962</td>
<td>-1350.20</td>
</tr>
<tr>
<td></td>
<td>(.151)</td>
<td>(-.328)</td>
<td>(-.280)</td>
<td>(-2.599)</td>
</tr>
<tr>
<td></td>
<td>(.045)</td>
<td>(1.178)</td>
<td>(-.835)</td>
<td>(3.506)</td>
</tr>
<tr>
<td>6. CPA</td>
<td>527.806</td>
<td>61.534</td>
<td>90.634</td>
<td>-1584.04</td>
</tr>
<tr>
<td></td>
<td>(.432)</td>
<td>(.239)</td>
<td>(.242)</td>
<td>(02.148)</td>
</tr>
<tr>
<td></td>
<td>(.691)</td>
<td>(-.673)</td>
<td>(.760)</td>
<td>(1.824)</td>
</tr>
<tr>
<td>17. OSHA</td>
<td>-314.283</td>
<td>562.078</td>
<td>764.157</td>
<td>-642.344</td>
</tr>
<tr>
<td></td>
<td>(-.898)</td>
<td>(2.262)</td>
<td>(2.144)</td>
<td>(-.917)</td>
</tr>
<tr>
<td>5. FECA</td>
<td>-1007.96</td>
<td>464.541</td>
<td>-680.625</td>
<td>3892.87</td>
</tr>
<tr>
<td></td>
<td>(-3.409)</td>
<td>(2.214)</td>
<td>(-2.262)</td>
<td>(6.583)</td>
</tr>
<tr>
<td>2. SRA</td>
<td>763.359</td>
<td>50.296</td>
<td>758.445</td>
<td>1155.51</td>
</tr>
<tr>
<td></td>
<td>(1.678)</td>
<td>(.156)</td>
<td>(1.637)</td>
<td>(1.269)</td>
</tr>
<tr>
<td>N-S Dummy</td>
<td>202.556</td>
<td>-77.393</td>
<td>500.723</td>
<td>-290.77</td>
</tr>
<tr>
<td></td>
<td>(.521)</td>
<td>(-.281)</td>
<td>(1.266)</td>
<td>(-.374)</td>
</tr>
</tbody>
</table>

\[ R^2 = .21 \]
The other result is that business seems to have been less effective in using contributions to influence legislation than were unions. Business contributions were less often significant in explaining voting than were union contributions; moreover, business contributions were also less influenced by the voting of Congressmen than were union contributions. These results are for the period 1972-74; it is possible that the increased political activism of business and the increased use of Political Action Committees would mean that business is now better skilled at using the political process than was the case some years ago. This would be a fruitful area for future research.
Footnotes

1. Chelius actually shows that accidents fell from the 1920s on, but with an increase in accidents in the 1960s. However, he finds that this increase was due to a change in the age composition of the labor force.

2. Simultaneous equations techniques would have been preferable. However, we have used such methods in the past and the results do not differ substantially from the results found here (Kau and Rubin, 1979b).

3. The table of coefficients is too lengthy for inclusion in this volume and may be obtained from the authors at The University of Georgia, Athens, Ga. 30601.
References

1. Barone, Michael, Grant Ujifusa, and Douglas Mattews, eds., Almanac of American Politics, Gambit, Boston, 1974
THE AVAILABILITY AND COST OF CREDIT AND VENTURE CAPITAL FOR SMALL BUSINESSES

David E. Fyffe
Georgia Institute of Technology

1. SUMMARY

Small businesses are a vital part of our economic system. Not only do they provide most of the employment and the industrial infrastructure; they also contribute much of the technology innovation. But, their major economic and social value (a subtle and infrequently mentioned point) is that without a continuing stream of new small ventures to challenge the existing powerful structure of corporate giants, a capitalistic economy cannot survive. These small businesses are necessary to maintain a healthy, competitive industrial system.

This study attempts to examine the availability and cost of credit and venture capital in Region IV with the purpose of providing recommendations to Federal and State policymakers. A summary of the major conclusions and recommendations follows.

Conclusions

- Credit for small business is available, but often at interest rates that exceed the return on investment of many small businesses.
- There is no evidence of internal malfunctions in the financial market.
- The relatively high cost of credit to small business is unintentionally, and perhaps unavoidably, aggravated by federal regulatory actions.
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- Paperwork requirements for SBA loans make this source inaccessible to some small businesses.
- Venture capital for small business start-ups is not usually available from sources other than the entrepreneur and his friends.
- States have not explored alternatives for providing small business venture capital.

Recommendations

- De-couple the availability and cost of small business loan funds at commercial banks from Federal Reserve regulatory actions.
- Encourage small business growth and reduce the need for external financing through tax exemption for reinvested earnings.
- Increase State and local activities to supply start-up funds for new ventures through industrial development authorities.
- Simplify SBA loan application requirements or else provide more effective assistance to small business owners in filling out these forms.
- Evaluate the effectiveness of Small Business Investment Companies in their role as suppliers of venture capital and long-term credit to small companies.

2. OVERVIEW

Small businesses play a vital role in the economic health of the nation. They provide most of the employment, develop much of the innovative technology, and maintain public confidence in our capitalistic system. Thus, there is justification for the mounting concern over the continuing decline in start-ups and growth of small businesses. The causes of this decline must be identified and alleviated.
Studies at the national level by Shapero et al. [11], Griggs [5], and Hoffman [6] all support the conclusion that a key factor in the industrial development of a community or region is the presence of an aggressive financial community. The availability of credit and venture capital is essential to the generation and growth of small businesses. Recognition of this fact has led to widespread criticism of governmental policies and regulations which affect business financing [3], [4], [8], [10]. In response, several research groups have attempted to examine the effectiveness of venture capital markets.

An analysis of factors affecting private investments in new products, processes, and services was prepared by the Diebold Group [12] for the National Science Foundation in 1974. This study sought to identify opportunities for government intervention in the form of providing incentives to improve the supply of venture capital to the process of technological innovation. The authors recommended a specific program of investment guarantees intended to attract private sector financing to new technology-based enterprises.

In 1974, Bean, Schiffel, and Mogee [2] examined the validity of assertions that an inadequate supply of capital for new and small firms was stifling technological innovation by such firms. Their investigation served chiefly to emphasize the paucity of information about the nature of the problem and the process of venture financing. They concluded that Federal intervention in the absence of such information would be unwise.

In 1976, the Charles River Associates [1] completed an analysis of venture capital market imperfections for the Experimental Technology Incentives Program of the National Bureau of Standards. This study "found
no evidence of substantial market imperfections that restrict the flow of funds to small technology-based firms," and concluded that "attempts to increase the flow of funds by direct government investments in small technology-based firms tend to displace private funds rather than increase the total flow of funds."

The Small Business Administration Task Force on Venture and Equity Capital for Small Business [9] issued a report in January 1977 citing evidence of increasing conservatism in the financial community. The Task Force made a number of specific recommendations for government intervention to alleviate small business financing problems. These recommendations are the best that have been published.

Objectives and Scope

This study examines the financing of small businesses in Region IV of the Small Business Administration. For the purposes of the study, a small business is any business with fewer than 500 employees. Other measures of size, such as receipts and total assets, are not considered. The objectives of the study are to determine the availability and cost of credit and venture capital to small businesses in the Region and to examine factors that influence the availability of financing for such businesses. The purpose is to provide information and policy recommendations for Federal and State actions.

The "availability" of credit is interpreted from the viewpoint of the small business owner to mean the accessibility of short-term credit and term loans for various purposes. Likewise, venture capital "availability" is interpreted as the accessibility of start-up funds from organized capital sources. Although there appears to be no firmly established definition of
venture capital, it is characterized as being high risk and having the principal objective of capital gains. Thus, the distinguishing characteristic of venture capital sources is an investment policy aimed at achieving most of their profit through capital gains. This is not to say, however, that venture capital firms never use debt. They often use convertible debentures and warrants in a financing package.

Sources of Data

Published literature contains a great deal of general information concerning sources and trends in small business financing. Virtually no specific information exists, however, with which to assess either the availability or cost of credit in the Region.

The primary sources of published data concerning commercial bank lending activities are the Federal Reserve System and the Federal Deposit Insurance Corporation. These data are aggregated by state for all banks. They show all commercial and industrial loans in one category, making it impossible to identify loan activity to small businesses. The annual financial reports of individual commercial banks provide information on loans, but, again, the data do not distinguish small business loans from other commercial and industrial loans. The Small Business Administration publishes aggregate statistics for the Region concerning its loan activities, but published information concerning loans made by other types of lending institutions is nonexistent.

Because of the lack of published data, information concerning the lending activities of commercial banks was obtained from interviews and from a survey questionnaire which was mailed to eighty major commercial banks in the Region. Information was obtained from commercial finance companies and industrial development authorities through interviews.
The only published information on venture capital investments is from publicly held venture capital firms and shows as little detail as legally permissible. Statistics on equity investments by privately held venture capital firms and individuals are unobtainable. Since small businesses are more likely to deal with Small Business Investment Companies in their search for equity capital, representatives of these institutions were interviewed.

Perhaps the most relevant evaluation of the availability and cost of credit and venture capital to small businesses is the overall perceptions of small business owners. Accordingly, a questionnaire was mailed to a random sample of approximately 100 small manufacturing firms founded within the last five years. These companies were asked to describe their experiences in obtaining start-up funding and credit. Approximately 30% of them responded.

**Financing Needs of Small Businesses**

Small business financing needs are related to the stages of business growth. Phase I is the initial start-up stage. In this stage, the company has made a feasibility study and has developed a business plan, but has not yet produced any products or services. "Seed money" is needed to get the business into operation and to establish a market. The nascent company needs funds for fixed investments, pre-production expenses, and working capital.

In Phase II, the fledgling company has started production, established a market for its product or services, and has an earnings record. At this stage, it is likely to need additional equipment and working capital in order to grow.

If the company is successful, Phase III growth may be substantial. Sales may increase rapidly. As a result, the company must enlarge
inventories, obtain more working capital to carry additional accounts receivable, and expand existing facilities and/or acquire new facilities. The need for new financing is urgent. The greatest risk at this stage is the temptation to increase the debt/equity ratio so that the company has debt servicing problems if business growth does not meet expectations.

The maturing Phase IV sees the company well capitalized but with needs to modernize plant and equipment, to develop new products, and to restructure long-term debt.

Sources of Business Financing

As discussed above, the financing needs of a small company change as it goes through the different growth stages. In Phase I, organized sources for start-up capital include venture capital companies and Small Business Investment Companies. In reality, however, venture capital must be furnished by the entrepreneur and/or friends, relatives, and other private sources. The sale of equity through public offerings of common stock is not an accessible source of capital for small businesses. Registration costs and red tape are prohibitive and underwriters are not interested in small offerings.

Long-term credit, for a year or longer, is used for plant and equipment expansion and modernization. Short-term credit is for less than a year and typically provides working capital to finance inventories and accounts receivable or carry the company through seasonal expenses. Credit sources for small businesses include the following:

- Commercial banks
- Commercial finance companies
- Trade credit
The typical small business looks first to a commercial bank for both short-term credit and term loans. A great deal of short-term credit to finance working capital needs and some term loans to finance equipment is obtained from commercial finance companies. These institutions also provide factoring services. While such loans are typically short-term credit, they are often "rolled over" as they mature and are part of the permanent working capital for the company. Other sources of loans for small business which will be discussed in detail are the U.S. Small Business Administration and Small Business Investment Companies. Since businesses rarely have access to funds of pension plan trusts and life insurance companies, these sources are omitted from the discussions.

3. AVAILABILITY AND COST OF CREDIT

Availability and Cost of Credit from Commercial Banks

The principal financial centers in Region IV are located in Atlanta, Miami, Winston-Salem, Memphis, and Louisiana. The large commercial banks in these areas account for most of the commercial and industrial loan activity in the Region.

Commercial banks are the principal source for small business loans, and a good banking relationship is the most valuable asset that a small business owner/manager can acquire. All of the companies contacted during this study had obtained short-term and/or term loans from commercial banks.
In most instances, these loans were short-term borrowings to cover working capital needs. However, loans for periods of three to seven years to finance equipment were not uncommon.

**General indicators of loan activity.** It is difficult to accurately assess the availability of commercial bank credit for small businesses. In order for credit to be available, the bank has to have funds and the propensity to lend. The supply of funds at commercial banks is determined by deposits and by money borrowed. These total funds are influenced by competition for deposits and the competitive attractiveness of alternatives for investments by depositors. The supply is also affected by the cost of funds borrowed by the bank. The funds available to lend are controlled by reserve requirements.

Beyond this control, however, is the willingness of the bank to make business loans vs. other forms of loans and investments. The most readily available measure of a bank’s willingness to make business loans is found in the loan/deposit ratio. Table I shows the ratio of commercial and industrial loans to total deposits for insured commercial banks in each of the states in Region IV. Since the category of commercial and industrial loans includes more than small business loans, only very limited inferences can be drawn from Table I. What does seem clear, however, is that the loan/deposit ratio is an indicator of the aggressiveness with which banks make loans. The ratios in Table I appear to correlate positively with the industrial growth in the respective states in the Region. As with most correlations, it is impossible to distinguish cause and effect.

Another measure of loan activity is the charge-off of business loans as a percentage of such loans. All else being equal, a higher charge-off rate indicates a more aggressive, risk-taking loan policy. Unfortunately,
Table 1
COMMERCIAL AND INDUSTRIAL LOANS VS. TOTAL DEPOSITS
(AMOUNTS IN THOUSANDS)

<table>
<thead>
<tr>
<th>State</th>
<th>Total Deposits</th>
<th>C &amp; I Loans</th>
<th>Ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>$11,968,065</td>
<td>$2,369,669</td>
<td>23%</td>
</tr>
<tr>
<td>Florida</td>
<td>30,407,007</td>
<td>3,935,467</td>
<td>13%</td>
</tr>
<tr>
<td>Georgia</td>
<td>14,950,139</td>
<td>2,805,901</td>
<td>19%</td>
</tr>
<tr>
<td>Kentucky</td>
<td>12,387,849</td>
<td>1,971,702</td>
<td>16%</td>
</tr>
<tr>
<td>Mississippi</td>
<td>7,885,596</td>
<td>1,075,335</td>
<td>14%</td>
</tr>
<tr>
<td>North Carolina</td>
<td>14,352,762</td>
<td>3,485,752</td>
<td>27%</td>
</tr>
<tr>
<td>South Carolina</td>
<td>16,263,717</td>
<td>2,920,497</td>
<td>18%</td>
</tr>
<tr>
<td>Tennessee</td>
<td>5,081,338</td>
<td>686,497</td>
<td>14%</td>
</tr>
</tbody>
</table>


The bankers contacted refused to disclose this information.

Banker's attitudes toward business loans. Business lending policies at commercial banks in the Region vary widely. All of the banks, of course, are interested in the industrial health of the areas which they serve. However, variability in lending conservatism is apparent in the range of responses to the following questions:

"What percentage of total overall financing for a small business do you believe should be ownership funds rather than borrowed funds of any type?" The majority of loan officers answered that 25-50% of business financing should be furnished by owners. Some, however, felt that 10% was
sufficient, and others wanted owners to supply at least 60%.

"What is the maximum percentage of permanent working capital (i.e., financing for larger inventories and/or receivables) do you think commercial banks can prudently provide?" Most respondents answered that approximately 50% was appropriate, but answers ranged from 30% to 80%.

"What, in your judgment, is the maximum percentage of plant expansion (land, factory space, warehousing) that commercial banks can prudently provide?" Approximately 75% was the most common response, but a few loan officers said 60% and one answered 90%.

"Do you think that commercial banks can safely provide funds needed to start a new business for which a feasibility study indicates an acceptable financial return?" Over four out of five answered "yes." The percentage of total funds which these loan officers felt that commercial banks could prudently provide ranged from 30-40% to 80-85%. This appears to be inconsistent with the experiences of small business owners/managers in obtaining start-up funds. It may, however, reflect the lack of a sound business plan in their preparations to obtain financing and the lack of collateral.

Such variability in the attitudes among lending officers of commercial banks has influenced the perceptions by small business owners/managers that credit for small businesses is not sufficiently available.

Most loan officers prefer collateralized short-term loans (90-120 days) and seem to agree that the loan should be approximately 75% of the value of the collateral. Long-term loans of one to five years are made to provide funds for equipment, and loans with maturities of five to ten years are made for acquiring land and buildings. Data from Region IV concerning the volume of short-term loans vs. long-term loans are not
available. On a national basis, the ratio of short-term to long-term commercial and industrial loans in the range of $1,000 to $92,000 is 7.8/1.

Bank lending officers in Region IV perceive an added risk in lending to small businesses compared with large, strongly established enterprises. Some feel that a term loan is not a sound means of financing expansion for a small business. More than half stated that business size should affect the maximum maturity of term loans. Almost all respondents stated that the fact that a business was small should affect whether the loan should be secured (by collateral, mortgage, or guarantee) and two-thirds held that it should affect whether amortization should be required.

There is no doubt that loan officers tend toward conservatism in small business loans. One loan officer admitted this and stated that he had never had a charge-off. He knew that losing a small, perhaps nuisance, account would not affect his career, whereas a bad loan would. It is also worth noting that all of the commercial banks furnishing information for this study had commercial loan departments, but only two had a department or section specializing in loans to small businesses.

Loan officers of commercial banks claim that credit is sufficiently available to qualified borrowers. They readily admit, however, that lending policies are sensitive to economic conditions and that when the economy dips or federal money managers decide to tighten credit, the small business owner feels the crunch first. His line of credit is reduced or disappears and loan money is difficult to find. If a loan is found, the cost and terms are often restrictive. At present, many banks are in a period of tight loan policies and are requiring strong collateral — one loan officer jokingly said, "Like cash."
Cost and terms of loans. According to domestic financial statistics of May 1979, the prime rate charged by banks on short-term business loans has climbed from 7.93% in June 1978 to 11.75% in April 1979. The average interest rate charged for short-term commercial and industrial loans in February 1979 was 12.27%. These national rates seem to hold in Region IV. Commercial banks in the Region report rates of "prime to 3% over," and small business owners reported that they paid prime plus 1% or 2% for short-term loans from commercial banks. Several reported "floating" rates of 1-2% above prime.

Long-term loans were reported nationally at 12.01% in February 1979, which also seems consistent with Region IV markets. The interest rate, however, does not give the full cost picture. Severe restrictions often are placed on the small business owner/manager as a condition of the term loan. These include restrictions on additional borrowings, working capital requirements, and the payment of dividends.

The SBA Role in Small Business Financing

When financing is not otherwise available on reasonable terms, SBA may guarantee up to 90% (or $350,000, whichever is less) of a bank loan to a small company. When questioned about their SBA-guaranteed loans, all bankers who responded stated that they were willing to make such loans but did not actively solicit them. Most stated that the SBA guarantee permitted approval of loans which otherwise should be rejected. One loan officer stated that his policy was to permit the SBA guarantee to "make up" for one deficiency in the loan application. A few loan officers claimed that the SBA guarantee should not permit approval of loans which otherwise should be rejected.
If a loan is not obtainable from a private lender, SBA may either participate with a bank in making the loan or make a direct loan. The SBA share of an immediate participation loan ordinarily may not exceed $150,000, and direct loans also may not ordinarily exceed that amount. The interest rates on SBA's portion of immediate participation and direct loans is limited to a rate established by statutory formula relating to the cost of money to the government. It is below the commercial bank rate.

In addition to Section 7-A loans, the SBA makes Development Company Loans, Displaced Business Loans, and Economic Opportunity Loans. The total SBA loan activity in the Region is shown in Table 2.

Most small business owners/managers in the Region have not had experience with SBA loans. Only one in four of the small businesses that furnished information for this study had obtained (or attempted to obtain) an SBA participation or direct loan. Their experiences were mixed but seem to indicate that SBA is very conservative and that much paperwork is involved. One owner/manager who obtained an SBA loan for expansion and working capital said that he was required to pledge all his personal and business assets for a loan which amounted to only 50% of the collateral. His comment, "I would never again borrow from SBA because of collateral requirements," indicates something less than a pleasant experience. Another respondent commented, "SBA reaction to request at start-up was very negative. Few small businessmen could possess sufficient expertise to complete forms and do projections."

SBIC and 301(d) SBIC Loans

Small Business Investment Companies (SBIC) were created by the Small Business Investment Act of 1958 as a vehicle for providing equity capital and long-term loans to small businesses. SBICs organized under Section 301(d) of the act specialize in small business concerns owned by socially or
Table 2
REGION IV - SBA LOAN ACTIVITIES

<table>
<thead>
<tr>
<th>Loan Type</th>
<th>Number of Loans</th>
<th>Amounts (Millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan Guarantees</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Participation Loans</td>
<td>13,300</td>
<td>$808.0</td>
</tr>
<tr>
<td>Direct Loans</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Development Company</td>
<td>844</td>
<td>85.0</td>
</tr>
<tr>
<td>Displaced Business</td>
<td>292</td>
<td>21.5</td>
</tr>
<tr>
<td>Economic Opportunity</td>
<td>2,206</td>
<td>31.8</td>
</tr>
</tbody>
</table>
| TOTAL                      | 16,651          | $946.3             

economically disadvantaged persons. The SBA licenses and regulates these companies and is authorized to leverage their private capital (of which there must be at least $150,000) up to a four-for-one basis under certain conditions. As of December 1978, there were 37 SBICs and 15 Section 301(d) SBICs in Region IV. The number of SBICs in each state in the Region and their total capital are shown in Table 3.

According to SBA literature, these SBICs "supply venture capital and long-term financing to small firms for expansion, modernization, and sound financing for their operations." Perhaps this statement accurately reflects the objective in establishing the SBICs, but the actual results are less than hoped for.

The SBIC is simply not a viable source of long-term credit for the typical small business owner/manager. None of the small businesses responding to the survey for this study had obtained SBIC financing, and interviews with
Table 3
SBICs AND 301(d) SBICs IN REGION IV

<table>
<thead>
<tr>
<th>SBICs</th>
<th>Number of Companies</th>
<th>Total Private Capital</th>
<th>Total Obligations to SBA</th>
<th>Total Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>4</td>
<td>$1,810,000</td>
<td>$1,100,000</td>
<td>$1,910,000</td>
</tr>
<tr>
<td>Florida</td>
<td>9</td>
<td>10,542,139</td>
<td>18,948,580</td>
<td>29,490,719</td>
</tr>
<tr>
<td>Georgia</td>
<td>8</td>
<td>12,823,094</td>
<td>31,074,500</td>
<td>43,897,594</td>
</tr>
<tr>
<td>Kentucky</td>
<td>2</td>
<td>1,800,000</td>
<td>2,000,000</td>
<td>3,800,000</td>
</tr>
<tr>
<td>Mississippi</td>
<td>4</td>
<td>2,609,213</td>
<td>2,239,822</td>
<td>4,849,035</td>
</tr>
<tr>
<td>North Carolina</td>
<td>3</td>
<td>3,863,265</td>
<td>8,457,403</td>
<td>12,320,668</td>
</tr>
<tr>
<td>South Carolina</td>
<td>4</td>
<td>2,814,659</td>
<td>7,033,500</td>
<td>9,848,159</td>
</tr>
<tr>
<td>Tennessee</td>
<td>3</td>
<td>2,407,198</td>
<td>1,799,750</td>
<td>4,206,948</td>
</tr>
</tbody>
</table>

Total: $38,669,568 $72,653,555 $111,323,123

301(d) SBICs

<table>
<thead>
<tr>
<th>State</th>
<th>Number of Companies</th>
<th>Total Private Capital</th>
<th>Total Obligations to SBA</th>
<th>Total Capital</th>
</tr>
</thead>
<tbody>
<tr>
<td>Alabama</td>
<td>0</td>
<td>$</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Florida</td>
<td>8</td>
<td>3,630,000</td>
<td>1,650,000</td>
<td>5,280,000</td>
</tr>
<tr>
<td>Georgia</td>
<td>2</td>
<td>829,222</td>
<td>700,000</td>
<td>1,529,222</td>
</tr>
<tr>
<td>Kentucky</td>
<td>1</td>
<td>500,000</td>
<td>500,000</td>
<td>1,000,000</td>
</tr>
<tr>
<td>Mississippi</td>
<td>1</td>
<td>150,000</td>
<td>150,000</td>
<td>300,000</td>
</tr>
<tr>
<td>North Carolina</td>
<td>1</td>
<td>500,053</td>
<td>564,000</td>
<td>1,064,053</td>
</tr>
<tr>
<td>South Carolina</td>
<td>0</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Tennessee</td>
<td>2</td>
<td>1,000,000</td>
<td>0</td>
<td>1,000,000</td>
</tr>
</tbody>
</table>

Total: $6,609,275 $3,564,000 $10,173,275
SBIC managers in the Region disclosed that their impact on the financing of small businesses is very slight.

In general, SBIC investment policies eliminate small companies, especially start-ups, as investment alternatives. Many SBICs have a minimum investment policy (e.g., $100,000). More importantly, the typical SBIC is looking for situations that offer the promise of an upside potential in the 500-1000% range over a five-year period. Everyone wants to get in on the ground floor of another Control Data Corporation. Because of this, the SBIC has no interest in the small business which has the potential for only modest growth and a good income for its owners and employees. When SBIC managers are asked, "How many deals do you look at for each one in which you invest?" the usual answer is "About one in a hundred survive the first screening and, of those, we invest in perhaps one in every twenty-five." In a given year, the SBIC may invest in only three or four new deals.

The favorite investment for the SBIC is one with as little downside risk and as much upside potential as possible. Therefore, most investments are secured by convertible debentures (convertible at a very nominal price) or a note with warrants to purchase common stock (at a very nominal price). Interest rates are about 2% above the prime rate. In spite of these investment policies -- or maybe because of them -- the typical SBIC has a modest 6-8% net investment income to average net assets. [1]

Industrial Development Authorities

Local and/or State industrial development authorities are authorized by statute in the states of Region IV. The statutes and the operations of these development authorities differ widely from state to state. In general, statutes provide that development authorities may issue tax-exempt revenue
bonds (the usual buyers are commercial banks) for specific development projects such as the development of industrial sites and industrial parks and the construction of plants. The development authority then leases or sells the facility to a business (not necessarily a small business), and the proceeds are used to retire the bonds. Georgia Statutes also permit the local development authority to issue revenue bonds and to "extend credit or make loans to any person, firm, corporation or other industrial entity for the planning, design, construction, acquisition or carrying out of any project."

Information concerning the amount of financial assistance extended to businesses by development authorities is not available. None of the small business owners who provided input for this study had received such assistance.

**Commercial Finance Companies**

There is no way to know the volume of small business loans made by commercial credit companies. It seems likely, however, that these institutions play a much larger role in meeting the credit needs of small businesses than the published literature indicates. Bank loan officers report that commercial credit companies supply much of the short-term working capital needs and that "rolling over" these loans enables them to be used as permanent working capital. Based on responses of small business owners, commercial finance companies also provide loans for terms of longer than one year to finance equipment purchases. In fact, almost one half the small businesses that responded to the survey questionnaire had obtained equipment loans from commercial finance companies.

Interest rates for such loans are very high -- usually 4-6% above the prime rate. Commercial finance companies, in some states at least, are not restricted by state usury laws. Their interest rates are whatever the market will bear.
Further indicators that commercial finance companies are aggressive credit suppliers and that this is a lucrative business are the large number of companies and the fact that many large corporations have established subsidiaries for commercial credit operations. A partial listing of such companies in Atlanta includes Chrysler, Control Data, Ford Motor Company, General Motors, ITT, General Electric, Ingersoll Rand, International Harvester, International Paper, and Westinghouse. The major commercial finance companies, such as CIT, Citicorp, and Heller, also are located in Atlanta.

Other Sources of Business Credit

About two thirds of the small business owners consider trade credit an important source of working capital. There is no doubt that the extension of credit by suppliers reduces working capital requirements. Since trade credit is not an institutionalized source of business financing, however, it is not considered in this study.

4. AVAILABILITY AND COST OF VENTURE CAPITAL

Availability of Capital from Organized Venture Capital Sources

In spite of the fact that most publications on venture financing provide a long list of organized venture capital sources, they are not accessible to small businesses. The only source of start-up (Phase I) capital available to the small business entrepreneur are loans against personal assets, funds from friends and relatives, and investments by private investors. None of the small businesses that provided information for this study had obtained seed money from other than these sources.

As expected, the majority -- over two thirds -- had started their companies with capital obtained from savings or from bank loans against their personal
assets. Investments by friends and relatives and by private investors were tied for second place.

Venture capitalists reported that, except in unusual situations, they are not interested in start-ups. They believe that the risk is too great. It would be more accurate, however, to say that efforts to evaluate the risk in each "deal" would be prohibitively costly (perhaps impossible) and that they prefer to wait until a company has proven that: 1) management is capable, 2) it can produce a product, 3) there is a growing market for the product, and 4) the operation is profitable with the promise of rapid growth. The extent of these capabilities is usually apparent at the first expansion stage (Phase II or III).

**Investment Policies of Venture Capitalists**

Screening criteria for venture capital investment decisions are of two types, as follows:

**Policy criteria**
- Size of the investment
- Business line of the company
- Stage of development of the company
- Growth potential

**Venture criteria**
- Management capability and commitment
- The nature of the product
- The market
- Management technical skills
- Management marketing skills
- The market plan
Almost all investment opportunities come from referrals by banks, accountants, directors, and trusted contacts -- almost never from "walk-in" proposals.

Investment companies frequently limit individual investments to a specific maximum and/or minimum. SBICs, for example, are required to limit their investment in any one company to a maximum of 20% of their capital. Similarly, investment companies may restrict their investments to a particular industry. Among the 37 SBICs in the Region, only 21 have a diversified investment policy. Eight restrict their investments to grocery stores and five others are restricted to having at least 50% of their invested capital in real estate.

Cost of Venture Capital

In compensation for the risks of investing in a small business, the investment company wants the opportunity for an equity position as a condition of a collateralized loan at relatively high interest. The loan, however, may be subordinated. A typical deal is that which one manager described as his most recent SBIC deal. This investment was a seven year term loan at 2% above the prime rate with warrants to buy 20% of the company at a "nominal" price. In this case, according to the venture capitalist, the nominal price was book value at the time of the deal.

Federal Laws and Regulations and Venture Capital Availability

The evidence that small business start-ups in the United States have declined is indisputable, but the identified causes of this decline are not at all indisputable. Because venture capital is not readily available to small businesses, however, there is widespread criticism of Federal laws and regulations which reduce incentives for investors or otherwise inhibit investments in small businesses.
Employee Retirement Security Act of 1974 (ERISA). With good intentions, ERISA makes pension trustees personally liable for the prudence of their investment decisions. As a result, they are reluctant to invest in small companies and are forced to become conservative in choosing their portfolios. Small businesses have been cut off from this source of capital.

SEC regulations. Small firms do not often attempt the public offering of securities because of underwriting costs and restrictive regulations. As a partial remedy, the SEC created Regulation A, which facilitates securities offerings of $500,000 and less by exempting them from full registration. However, the requirements are still very complicated and expensive. Moreover, underwriters are not interested in offerings this small. As a result, small businesses are unable to obtain equity capital through public offering of common stock.

Rule 144 is intended to prevent the circumvention of registration requirements for securities offered on the open market. It provides that if the sale of stock by a "controlling" person is considered to be a "distribution," then the stock must be registered. The venture capitalist who has invested in a new venture and wants to liquidate his holdings may be considered to be a controlling person and thus is severely restricted by Rule 144. He and his associates must avoid selling more than 1% of their outstanding stock in any six-month period. This may have the effect of "locking in" his investment over many years.

IRS capital gains tax. The capital gains tax is lower than ordinary income tax for most taxpayers and is intended to provide an incentive for investment. However, it is under continual attack in the Congress and has been increased. Its value as an investment incentive is severely weakened.
5. SMALL BUSINESS OWNER/MANAGER PERCEPTIONS

Most small business owners are convinced that credit is not sufficiently available for them. All of those who furnished information for this study had, at one time or another, borrowed from one or more sources of credit. Approximately two thirds stated that, in their opinion, credit was not sufficiently available. Their perceptions are as follows:

- Lending institutions discriminate against small businesses -- loan restrictions are more stringent, terms are shorter, and interest rates higher than for large companies.
- Banks are unnecessarily conservative in making small business loans.
- In periods of tight money, small business financing disappears quickly.
- Small to medium-size businesses often have loan needs which are too large for all but the largest commercial banks and too small for major financial institutions.

About 20% of the small business owners, on the other hand, believed that credit is sufficiently available. In all cases, these individuals had not borrowed extensively and apparently were well capitalized. Their borrowing experience consisted largely of short-term loans at commercial banks and/or SBA immediate participation loans.

Venture capital seed money from organized sources is unavailable to small business entrepreneurs. A few respondents stated that they had furnished all start-up funds themselves and had not approached outside sources. The remainder had obtained start-up money from private sources -- including friends and relatives -- and stated emphatically that they had experienced problems.
6. CONCLUSIONS AND POLICY RECOMMENDATIONS

The stated objective of this study was to examine the availability and cost of credit and venture capital for small businesses in Region IV. The purpose was to provide a basis for Federal and State policy recommendations.

Conclusions

Credit for small business is available but often at interest rates which exceed the return on investment of many small businesses.

Although the conservative loan policies of many commercial banks eliminate worthy borrowers, credit is available from an aggressive commercial credit industry that is ready and eager to supply funds at interest rates of 4-6% over the prime rate. This high interest may exceed the return which a small business owner is willing to accept on his invested capital. For such a small business, affordable credit is not available.

The relatively high cost of credit to small businesses is a result of the supply and cost of funds to lenders, competition for scarce funds available to lend, and risk perceptions of lenders. There is no evidence of internal imperfections in the financial market.

In a free market, prices are established by the competitive actions of all sellers. Assuming that the cost of the commodity itself is the same to all sellers, pricing differences can be accounted for by differences in operating costs and in acceptable profit margins. The financial loan market operates as any other market except that: 1) the notion of risk is introduced and 2) the supply and cost of the commodity are controlled by Federal actions. Because of risk, the price for the same commodity is not the same for all customers of a given lender. The difference in interest rates for loans to small businesses compared with those charged large businesses reflects the additional risk as perceived by the lender. No
data are available to determine whether or not the interest differential for small business loans is justified by a higher rate of charge-offs.

Other researchers who have examined the problems of small business financing have concluded that no imperfections exist in the internal operations of financial markets. This study, likewise, does not find evidence of internal malfunctioning.

The relatively high cost of credit to small businesses is unintentionally, and perhaps unavoidably, aggravated by Federal regulatory actions.

The small businessman who needs financing is forced to turn to the higher-cost commercial finance companies if funds are not available from a commercial bank. Availability and cost of funds to commercial banks are tightly controlled by Federal Reserve Bank actions. The principal regulatory actions are: 1) adjustments of commercial bank reserve requirements against both time deposits and demand deposits, and 2) manipulations of Federal funds rates which increase or decrease the costs of funds to commercial banks. Increases in reserve requirements greatly reduce the amount of lendable funds at commercial banks.

Federal Reserve regulatory actions are in response to overall economic pressures in the nation and are planned to stimulate or to "cool" the national economy as needed. These actions, however, do not equally affect all the users of funds. Unfortunately, the small business owner stands at the end of the line. If there are not enough funds to satisfy all loan requests, large customers receive preference. The result is that small regulatory actions that do not affect the financing of large companies may squeeze the life out of small businesses.
Paperwork requirements for SBA loans make this source inaccessible to some small businesses.

Although the SBA loan programs have helped and are helping thousands of small businesses in the Region, other firms find the "red tape" excessive. Opinions and comments concerning SBA loan requirements were not expressly solicited during the study, yet some 15% of those who responded to the survey questionnaire stated that they found SBA paperwork too burdensome.

Venture capital for small business start-ups is not available from sources other than the entrepreneur and his friends.

Seed money from organized venture capital sources is not available to the vast majority of small business ventures. The total capital of over $120 million among the 52 SBICs in the Region is only a drop in the bucket compared with financing needs. Moreover, SBICs tend to stay clear of seed money deals. They also seek deals which offer at least the possibility of very rapid growth. The typical small business venture does not qualify.

At the State and local levels, industrial development authorities are concerned with infrastructure development and promotional efforts to attract new companies. States have not explored alternatives for providing small business venture capital.

The operations of State and local development authorities in the Region are not well known. In most states, there is no central coordinating agency and thus no knowledge of the total activity that is underway. In some states, development authorities do not utilize their authorizations to provide financial assistance to develop industry. It appears that this source of financing could play a much more important role than at present.
Policy Recommendations

1. **De-couple the availability and cost of small business loan funds at commercial banks from Federal Reserve regulatory actions.**

   Commercial banks should be authorized to issue Small Business Investment Bonds. The proceeds of the bonds would be used exclusively for small business loans. Small businesses that purchase bonds would be permitted to defer Federal income taxes on the funds invested for as long as the bonds were held. Taxes would be paid at the time the bonds were converted to cash unless the money was reinvested in the business (see Recommendation 2).

   If handled in this manner, the bonds would not draw a significant amount of funds from home mortgage sources. They would, on the other hand, encourage small businesses themselves to provide funds for small business loans and reduce their dependence on borrowed funds by permitting small businesses to build untaxed cash reserves in anticipation of future capital needs.

   Most importantly, these bonds would not be subject to reserve requirements and, therefore, would serve to reduce the sensitivity of small business loan funds to Federal Reserve regulatory actions.

2. **Encourage small business growth and reduce the need for external financing through tax exemption for reinvested earnings.**

   Investment credits provided by current tax laws are intended to encourage small business investment. However, the present investment tax credit is not an effective motivator for small business investment. The amount of tax credit is insufficient to provide a strong incentive and many types of business investment do not qualify. Moreover, like the remainder of IRS regulations, it is incomprehensible to everyone and the small
businessman simply depends on his accountant to take advantage of it if it will save taxes.

The concept of tax exemption for reinvested earnings is simple -- if you put business earnings to work in the business that produced them, you do not have to pay taxes.

3. Increase State and local activities to supply start-up funds for new ventures through industrial development authorities.

State industrial development authorities are active in assisting the development of industrial infrastructure and in promotional efforts to attract industry. They are not taking advantage of their authorizations to issue tax-exempt revenue bonds for development purposes. Moreover, statutes in different states vary widely. An effort should be made to develop a model statute based on the experiences of different states, and industrial development authorities should take a more active role in supplying venture capital.

4. Simplify SBA loan applications requirements or else provide more effective assistance to small business owners in filling out these forms.

This recommendation is not intended to imply that the SBA does not provide assistance to small businesses. However, the number of owners who perceive this as a problem indicates that action is needed.

5. Examine the present role of SBICs to determine if changes should be made to improve their record as suppliers of small business venture capital or if SBA support should be discontinued.

It seems clear that SBICs are not as effective as anticipated. It is not easy to determine just what is being accomplished, but their continued support should depend on an assessment of effectiveness in supplying the needs of small businesses with venture capital and long-term credit.
References


1. BACKGROUND AND PURPOSES

The background leading up to this study was given in the introduction to an article appearing in Nation's Business. It stated:

Small business is in a state of declining economic strength, this should be a concern for all Americans, especially national leaders of both government and business.

This is the warning issued in a special report on the state of small business prepared by the Chamber of Commerce of the United States and sent to President Carter and key leaders in Congress.

Actions of government are major reasons for the decline, the report says, especially in the areas of taxation and of regulation, with its accompanying paperwork. Also cited is the failure to curb inflation.

The report advocates corrective steps in these areas and urges the President to call a White House conference on small business.

Such a conference, the report says, could:

- Increase public awareness of the importance of small business.
- Examine specific problems of small business.
- Explore possible government actions to encourage the growth of small business ["Improving the State of Small Business," 1978, p. 38].

The importance of small business to the nation can be realized from the following quote:

Small businesses are crucial to the American way of life. Across the country they comprise 97 percent of all incorporated and
unincorporated businesses. Their operations generate more than half of all business receipts, and they employ more than half of the private work force in the U. S. [Nydegger and Blum, 1978, p. 87].

There were several purposes for conducting this study. One purpose was to identify the internal and external (to the firm) items of information which will enable small business to operate more efficiently and effectively. Another purpose was to identify those topics which, if investigated, could be of major importance to small business. Thus, government-funded research could be directed to the topics identified.

To accomplish these purposes, a study was conducted involving small business in Region IV, as identified by the Small Business Administration. The Region includes the following states in the Southeastern United States: Alabama, Florida, Georgia, Kentucky, Mississippi, North Carolina, South Carolina, and Tennessee. The results of the study will be given. They lead to recommendations regarding actions that might be taken. Recent literature on small business will be integrated in with the recommendations.

2. THE STUDY

A questionnaire was sent to a random sample of 400 owners of small businesses in the Southeastern United States. The names were supplied by offices of the Small Business Administration in Region IV. Of the 400 questionnaires sent, 136 usable responses were returned. This represents a response rate of 34 percent. A comparison of later responses with those received earlier indicated no significant difference in response pattern. Thus, the data seem to be unbiased. In other words, those who did not respond probably would have responded similarly to those who did respond.
The questionnaire contained four basic opportunities for response. They were:

1. Which of the following *internal* items of business information would be most useful to the management of your business? Allocate a total of 99 points among them in terms of their usefulness.

2. Which of the following *external* items of business information would be most useful to the management of your business? Allocate a total of 99 points among them in terms of their usefulness.

3. Assume that the federal government intends to fund research projects pertaining to small business. Allocate a total of 99 points among the topics you believe should be investigated in terms of their importance to your business.

4. Please give any comments you would care to make concerning the business information and research needs of small business.

Each of the first three questions contained eight suggested items which the respondent could select. The nature of these items is identified in Tables 1, 2, and 3 to be described later. In addition, there were two spaces in which the respondent could describe other items which were not included in the listing.

Other data on the characteristics of companies represented were also asked for in the questionnaire. These data are described in the following section.
3. RESULTS OF THE QUESTIONNAIRE

Characteristics of Companies

The characteristics of the companies represented by respondents were as follows:

<table>
<thead>
<tr>
<th>Business form:</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporation</td>
<td>104</td>
</tr>
<tr>
<td>Proprietorship</td>
<td>27</td>
</tr>
<tr>
<td>Partnership</td>
<td>4</td>
</tr>
<tr>
<td>Trust</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>136</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Type of business:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Service</td>
<td>43</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>41</td>
</tr>
<tr>
<td>Retail</td>
<td>27</td>
</tr>
<tr>
<td>Wholesale</td>
<td>12</td>
</tr>
<tr>
<td>Construction</td>
<td>11</td>
</tr>
<tr>
<td>Banking</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>136</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Average annual sales and/or service revenue:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Over $1,000,000</td>
<td>56</td>
</tr>
<tr>
<td>Between $500,000 and $1,000,000</td>
<td>26</td>
</tr>
<tr>
<td>Between $100,000 and $500,000</td>
<td>37</td>
</tr>
<tr>
<td>Less than $100,000</td>
<td>17</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>136</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Location:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Large city (over 500,000 population)</td>
<td>19</td>
</tr>
<tr>
<td>Medium city (from 50,000 to 500,000)</td>
<td>47</td>
</tr>
<tr>
<td>Small city or town (under 50,000)</td>
<td>53</td>
</tr>
<tr>
<td>Suburbs</td>
<td>6</td>
</tr>
<tr>
<td>Rural</td>
<td>10</td>
</tr>
<tr>
<td>Other--airport</td>
<td>1</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>136</td>
</tr>
</tbody>
</table>

Other company data were also reported. The average number of years the business had been in operation was 22 years. The average number of persons engaged in the business (management and employees) was 50.

Useful Internal Items of Business Information

The results for Question 1 regarding the most useful internal items of business information to management are given in Table 1.

An explanation of the format of the tables is in order. The first column shows the total number of respondents selecting the item. The second column shows the total number of points assigned to the item. Remember that
Table 1  
INTERNAL ITEMS OF BUSINESS INFORMATION  
WHICH WOULD BE MOST USEFUL TO THE  
MANAGEMENT OF YOUR BUSINESS  

<table>
<thead>
<tr>
<th>No. Selecting This Item</th>
<th>(2) Total Points Assigned To This Item</th>
<th>(3) Avg. Pts. By Those Selecting This Item</th>
<th>(4) Avg. Pts. When Total Pts. Divided By Total Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Cash forecast for coming period</td>
<td>99</td>
<td>1,952</td>
<td>20</td>
</tr>
<tr>
<td>2. The effects of inflation on your average current asset balances</td>
<td>93</td>
<td>1,864</td>
<td>20</td>
</tr>
<tr>
<td>3. Income after inflationary effects (real income)</td>
<td>87</td>
<td>1,732</td>
<td>20</td>
</tr>
<tr>
<td>4. Alternative means of accomplishing your business goals</td>
<td>84</td>
<td>1,793</td>
<td>21</td>
</tr>
<tr>
<td>5. The cost of complying with government regulations</td>
<td>82</td>
<td>1,671</td>
<td>20</td>
</tr>
<tr>
<td>6. Budget (pro forma financial statements) for coming year</td>
<td>73</td>
<td>1,401</td>
<td>19</td>
</tr>
<tr>
<td>7. Financial statements for current year (and prior years)</td>
<td>58</td>
<td>1,363</td>
<td>24</td>
</tr>
<tr>
<td>8. The cost of wasting energy resources in your business</td>
<td>57</td>
<td>704</td>
<td>12</td>
</tr>
<tr>
<td>9. Other</td>
<td>13</td>
<td>445</td>
<td>34</td>
</tr>
</tbody>
</table>
each respondent was asked to allocate a total of 99 points among the item in each question. The purpose for doing this was to gain an understanding of the strength or magnitude of their preference for a particular item in relation to the other items selected. Column 3 is the average number of points assigned to an item by those selecting that item. Column 4 shows the average number of points for an item when the total number of respondents to the questionnaire (136) is divided into the total points assigned to an item. In other words, those who did not select an item could be said to have consciously assigned a point value of zero to that item.

Table 1 shows that the most valuable internal items of information are a cash forecast for the coming year, the effects of inflation on the average current asset balances, income after inflationary effects, alternative ways of accomplishing business goals, and costs of complying with government regulations. The items are listed in descending order in terms of the number of respondents selecting that item. An argument could be made that item 4 should be ranked ahead of item 3 since more total points were assigned to it. Even those items ranked in the 6th through 8th positions received considerable support. Items mentioned in the "Other" category included inventory control, daily profit and loss statement, sales (market) forecast, cost accounting data, and adequate financial advice. If any of these items had been included in the list suggested to respondents, they probably would have received more support.

Useful External Items of Business Information

The results for Question 2 regarding the most useful external items of business information to management are given in Table 2. The columns are
Table 2
EXTERNAL ITEMS OF BUSINESS INFORMATION
WHICH WOULD BE MOST USEFUL TO THE
MANAGEMENT OF YOUR BUSINESS

<table>
<thead>
<tr>
<th>No.</th>
<th>Selecting This Item</th>
<th>(2) Total Points Assigned</th>
<th>Avg. Pts. By Those Selecting This Item</th>
<th>(4) Avg. Pts. When Total Pts. Divided By Total Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>A summary showing financial ratios of companies similar to yours</td>
<td>104</td>
<td>2,146</td>
<td>21</td>
</tr>
<tr>
<td>2</td>
<td>Costs and means of borrowing by businesses similar to yours</td>
<td>103</td>
<td>2,068</td>
<td>20</td>
</tr>
<tr>
<td>3</td>
<td>A general economic forecast for coming period</td>
<td>100</td>
<td>2,086</td>
<td>21</td>
</tr>
<tr>
<td>4</td>
<td>Costs and means of obtaining investment capital in businesses such as yours</td>
<td>97</td>
<td>1,825</td>
<td>19</td>
</tr>
<tr>
<td>5</td>
<td>A summary and interpretation of government regulations affecting small business</td>
<td>90</td>
<td>1,838</td>
<td>20</td>
</tr>
<tr>
<td>6</td>
<td>A knowledge of sponsored (low cost) programs to strengthen your management skills</td>
<td>77</td>
<td>1,069</td>
<td>14</td>
</tr>
<tr>
<td>7</td>
<td>A summary showing use of energy in businesses similar to yours</td>
<td>53</td>
<td>565</td>
<td>11</td>
</tr>
<tr>
<td>8</td>
<td>A summary of surplus labor (by skills) in various geographic areas</td>
<td>44</td>
<td>449</td>
<td>10</td>
</tr>
<tr>
<td>9</td>
<td>Other</td>
<td>8</td>
<td>291</td>
<td>36</td>
</tr>
</tbody>
</table>
similar to those in Table 1. The most useful external items are a summary showing financial ratios of similar companies, costs and means of borrowing by similar businesses, a general economic forecast for the coming year, costs and means of obtaining investment capital, and a summary and interpretation of government regulations affecting small business. Again, items ranked in the 6th through 8th positions also received considerable support. Items listed in the "Other" category included a true forecast of raw material cost, how to protect yourself against harassment by OSHA and unions, and how to increase productivity.

Areas of Research Important to Small Business

Table 3 shows the results of Question 3 regarding areas of research which are important to small business. The columns are similar to those in Tables 1 and 2. Again, all of the suggested topics received some support. The ones receiving the most support were ways to reduce government regulation of small business, ways to simplify the federal income tax law, ways to reduce the cost of borrowing for small business, the effect of increasing the minimum wage on small business, means of increasing productivity, and the effects of inflation on small business. Again, items ranked in the 6th through 8th position also received considerable support. Topics included in the "Other" category were how to establish ideal customer credit policies, ways to protect secondary lien holders, ways to stop government deficit spending, how to stop payroll reports on federal jobs, how to find skilled employees, and how to develop new products. Several respondents stated that the federal government is already researching more than the taxpayer can pay for.
Table 3

AREAS OF RESEARCH WHICH COULD BE FUNDED BY THE FEDERAL GOVERNMENT WHICH WOULD BE MOST IMPORTANT TO YOUR BUSINESS

<table>
<thead>
<tr>
<th>No.</th>
<th>Selecting to This Topic</th>
<th>Total Points Assigned (2)</th>
<th>Avg. Pts. When Total Points Divided by Total Respondents (4)</th>
<th>Avg. Pts. By Those Selecting This Topic (3)</th>
<th>(2) ÷ (1)</th>
<th>(2) ÷ 136</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Ways to reduce government regulation of small business</td>
<td>108</td>
<td>3,067</td>
<td>28</td>
<td>23</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Ways to simplify the federal income tax law</td>
<td>97</td>
<td>1,920</td>
<td>20</td>
<td>14</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Ways to reduce the cost of borrowing for small business</td>
<td>88</td>
<td>2,025</td>
<td>23</td>
<td>15</td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>The effect on small business of increasing the minimum wage</td>
<td>78</td>
<td>1,474</td>
<td>19</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Means of increasing productivity</td>
<td>77</td>
<td>1,609</td>
<td>21</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Effects of inflation on small business</td>
<td>75</td>
<td>1,202</td>
<td>16</td>
<td>9</td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Equity capital formation and maintenance in small business</td>
<td>53</td>
<td>928</td>
<td>17</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Ways to conserve energy resources in a small business</td>
<td>43</td>
<td>527</td>
<td>12</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>9.</td>
<td>Other</td>
<td>11</td>
<td>354</td>
<td>32</td>
<td>3</td>
<td></td>
</tr>
</tbody>
</table>
Comments Given on Open-Ended Question

Respondents were asked to give any other comments concerning the business information and research needs of small business. Representative comments are given here to give a further indication of the beliefs of the respondents. They are categorized and numbered to separate one from another. Also, some minor editorial changes have been made.

Too much regulation and paperwork.

1. Too much paperwork -- one-man business has to hire another man just to take care of the paperwork.

2. The small business needs some relief from government regulations. We need a conservative running the country instead of a liberal. The reason I say that is as follows: Last year my gross sales were the highest in my company's history and I lost over $100,000. We need some relief from the high prices we have to pay for insurance.

3. Small businesses serve limited areas. The more rules and regulation they are strapped with, the higher the cost of operation. Therefore, they cannot compete with large chains vying for the same consumer dollar. Small businessmen are the backbone of our nation. We are slowly driving them out of business with government controls and regulations.

4. We are having to spend too much of our laboratory, research time, and money changing formulations to meet government regulations. This is nonproductive time and money. The additional burden of government regulations is killing small manufacturers. The giants are all that will be left.

5. Starting in business I needed a lot of information on how to handle government regulations. Now we don't need information from government -- we need simplified regulations.

6. My business depends on trucking a finished product. The ICC regulations are very harsh and very expensive for a small company to comply with. The ICC and Department of Transportation force businesses to waste huge amounts of needed fuel.

7. The biggest problems are complying with government regulations and borrowing money. Banks have little concern for small manufacturing companies. They don't understand their needs and don't care to learn. Transportation is a real problem in rural areas. Also, the paperwork load and insurance costs are tremendous for a small company. We don't have a staff of CPA's, lawyers, etc. to do all these things necessary to keep up to date.
8. Our two most troublesome areas are government regulations and energy.

9. SBA loans are too complicated to obtain. Banks do not want to go through the bother and tend to urge businessmen to simply accept bank loans rather than go through the hassle of dealing with the SBA.

10. Government red tape is killing small business.

11. We need a simpler way to operate. Our company owns its own tractors and trailers. They are used only to deliver our products. Licenses and fuel permits required by federal and state governments and the quarterly reports we must file are administrative burdens.

12. Small business needs a tax break and help in reducing the amount of paperwork. We cannot continue to pay taxes and be left with nothing but worn out equipment and inventory.

13. We have the knowledge, expertise, and ability to operate a small business as demonstrated by 30 years of experience. We cannot continue to survive if Government controls and regulations continue to escalate. If knowledgeable people had contrived to destroy small business in the U.S., I don't believe they could have been more effective than the U.S. Government and its bureaucrats have been for the last 30 years.

14. I feel any research done by the federal government will create 10 more forms for us to fill out.

15. The single most cost effective problem in a small construction business is GOVERNMENT (primarily Federal) regulations, guidelines and "aids"!

16. If we could get the government out of our lives and off our backs, we wouldn't need the Small Business Administration!

Additional information needed.

17. We need to know:

a. ways to compete with larger companies in some field of business.

b. local geographical wage rates and ratios for sales personnel and skilled and semi-skilled technicians.

c. ideal ratios for businesses doing $100,000, $250,000, $500,000, $1,000,000 sales (e.g., profit to sales dollar; wages, inventory, etc. to sales dollar).

18. Commerce Department needs to assist those in small business in entering export market. Should we do so directly or use an agent or distributor?

19. a. The information needed for the operation of a small business is available from many sources. Not many people know how to search out these sources of information.
b. Results of undercapitalization should be made known.

c. Insurance cost should be reduced (primarily workmen's comp).

d. We need to know how to live on nothing for 8 years while trying to be successful in a small business.

e. We need to know the potential of the business.

f. We need to know how to evaluate various locations in which to operate our business.

20. We need to know:

a. How to cheaply figure unit costs;

b. How to afford OSHA and FDA requirements; and

c. How to afford equipment to keep up with the "BIG BOYS."

21. If studies would be specific (with reference to specific areas of production/manufacturing) and if the studies were specific to one industry rather than a broad range of industries -- then they would be useful. At present, many industries are combined in many studies and the results are of little value to the working manager.

22. The small business will soon be obsolete ($500,000 and under) due to the technology required to compete. Small business needs research, capital for new equipment, and availability of working capital, from sources that can furnish these needs at reasonable cost.

Less information needed from government.

23. Small businesses can get better information from their local banks, S & L, Chamber of Commerce, etc. than anything furnished by the U.S. Government due to the fact that the government information covers too wide an area. The government could do better by not spending the tax money this way. In fact the government cannot give an economic forecast that is of any use to small business.

24. Lots of government information and research is furnished by trade organizations and is more accurate than what the government furnishes. I surely do not want more government furnished reports if I have to fill out more forms, etc.

Other.

25. A study of benefit derived from reduction in government charity should be made -- that is, by what amount will we gain in both taxes saved and increased production if unemployment, welfare, workmen's compensation, food stamps, minimum wage, etc. were reduced and made available only to persons not capable physically or mentally of productive employment.
26. Government needs to look at the working hours of construction workers. It benefits the out-of-town worker to work (4) ten hour days to get 40 hours. On government jobs we cannot do this because of laws that state all hours over 8 hours in a day are at time and half rates. The result is the worker has to spend an extra day away from his family. If he could work 10 hours per day the employee would not have to pay the extra day travel and both labor and management would benefit from this. There is also the problem of an out-of-town worker not having anything to do after he works his 8 hours. Usually he goes to his motel and is unoccupied until work time next day.

Government needs to become more realistic concerning actual working conditions of small business before establishing its regulations.

27. The SBA is not for the small business.

28. a. Require smaller bonds for small businesses. I could have done 4 times as much work if I could have gotten a bond.

b. Stop bidding big jobs that could be bid in 3 or 4 smaller jobs so small business could bid.

c. Don't advertise jobs over $2,000,000 as "Set Aside for Small Business." Small businesses cannot bond jobs over $2,000,000. Most small businesses are restricted by their bonding company to bid on jobs of under $500,000.

d. Should stop small businesses from bidding jobs for big businesses for a small percentage. We know this happens because the small businesses that have been bidding the jobs for the big businesses are limited to less than $700,000 in bonding power by the bonding company.

e. Should stop bidding several different kinds of work under one contract to large businesses. They bid the work for a high price and then force small businesses to take the work too cheap. If small businesses don't take the work for way below the original bid price, the big businesses do the work themselves. A good example is the Tenn.-Tom Bigbee Waterway in Mississippi. I have been in business for 25 years and have never made any money doing subcontracting.

One cannot help but note the anger displayed in some of the comments. Much of the anger is directed at the federal government for too much regulation, too much paperwork, and for providing the wrong kind of information. A fairly wide-spread belief is that reducing the government regulation of small
business would improve the climate for small business dramatically.

4. DISCUSSION OF THE RESULTS

Internal Information

The kinds of internal items of business information which were described as being most useful in Table 1 can be generated by competent employees within the organization or by outside consultants. One of the primary sources of outside expertise can be an accountant. A survey conducted in England revealed, for instance, that "37% of small firms first turn to their accountant when they need help" [Back, 1977, p. 52]. (Solicitors and bank managers were next in importance, 15% each). R. D. Back urged English accounting firms to make themselves increasingly available to small business to provide sound financial advice. Possibly accounting firms and other competent advisors in the United States should be encouraged to do likewise.

External Information

Financial ratios. Certain external items of business information were reported in Table 2 as being most useful. One was a summary showing financial ratios of similar companies. Possibly the SBA could gather and publish such data assuming that some trade association is not already doing so.

Raising capital. Two other items which ranked highly were costs and means of borrowing and of obtaining equity capital. The problem is likely to become even more serious in the future. A report of the National Association of Securities Dealers Special Committee on Small Business Financing concluded "that by 1985, half of all stocks in the country will be owned by institutional investors, compared with 41% in 1975, 30% in 1970 and 26% in 1960. Such institutions rarely consider investment in small and medium sized companies" [The Washington Scene, p. 3].
An omnibus small business bill which was vetoed in 1978 by President Carter would have reduced the cost of raising capital for small business. Its features were described as follows:

... the bill would have authorized the SBA to license a new type of small business investment company (SBIC) in an effort to help small firms get equity capital for growth.

Under this provision, venture capital SBICs could have borrowed from the federal government at a 4 per cent interest rate, and then lend this money to small businesses at a 9 per cent rate. In return, the venture capital SBICs would have given to the federal government 15 per cent of all realized capital gains.

Other provisions of the vetoed bill would have allowed the SBA to grant disaster loan rates of 3 per cent for losses up to $55,000 on homes and 5 per cent for losses up to $250,000 for business property. The bill would also have exempted firms with 10 or fewer employees from Occupational Safety and Health Administration requirements, which force companies to maintain a log of occupational injuries and illnesses. It also would have codified an existing law that prevents OSHA from fining small businesses (10 employees or less) that have no more than 10 worker safety violations [Carter Vetoes Omnibus Bill To Aid Small Business, 1978, p. 2].

Perhaps some similar legislation could be passed which would be perceived by all to be less inflationary. Also information could be disseminated on any other existing sources of debt or equity capital which might be available to small businesses. One respondent also recommended simplifying the SBA loan procedure so that banks would be more willing to become involved in these transactions.

One seemingly successful effort at raising capital for small businesses is that of the National Development Council (NDC). It was described as follows in a recent article:

The NDC, founded and run by 39-year-old Samuel S. Beard, a former aide to the late Senator Robert F. Kennedy, specializes in finding long-term financing for small, successful businesses in
urban areas. Since 1970 its small staff of expert loan packagers has put together 426 deals totaling $151 million from both government and private sources. Only 3% of these loans have defaulted, a better record than that of the Small Business Administration's loan program, which loses 5% of its loans.

In March, three federal agencies -- the SBA, the Economic Development Administration, and the Housing & Urban Development Dept. -- agreed to fund the NDC in a $700,000 pilot program designed to show 25 cities how to find long-term federal and private financing for small, hometown businesses. Surprisingly, federal officials say that even many big cities lack such expertise now.

A prime attraction of the NDC program is that, unlike the Administration's proposed $12 billion National Development Bank, it requires no new legislation. Cities can use existing HUD block grant funds to add trained loan packagers to their development staffs. Both the SBA and the EDA already offer long-term loans and loan guarantees for small business investments in urban real estate and fixed assets. But complex requirements have discouraged their use to the point where less than 10% of the SBA's $6.8 billion in outstanding loans and guarantees have terms of more than 10 years.

The NDC, however, has made a science of slashing through the red tape ensnaring government loan programs ["Keeping Small Business in Town," 1978, p. 65].

Efforts by the federal government to assist small businesses in raising capital often are hampered by rigid requirements, red tape, and lack of adequate publicity. An example is the effort to assist small business to finance pollution control equipment. The details are as follows:

in 1976 Congress amended the Small Business Investment Act of 1958 to help small businesses (assets not exceeding $9 million, net worth not exceeding $4 million, and average net income for two preceding years not more than $400,000) finance pollution abatement facilities.

The program, which carries a 100% guarantee by the Small Business Administration (SBA), places an AAA rating on the issues and enables a firm or a combination of firms to float a pollution control revenue bond at interest costs of about 6 1/2%, compared with about 11% for long-term bank financing.

The requirements under the law are strict, however. An applicant must be independently owned and operated, not a leader in its field, meet specific employee guidelines, be at an operational disadvantage
in regard to construction or financing of pollution abatement equipment, and prove the need for a facility to help prevent or reduce noise, air, solid waste, or water pollution.

Mr. Gillow and other observers point out that not many companies have participated in the program, despite its obvious merits. "Very few companies in the coke industry would qualify in terms of size," he reasons.

Adds John H. Noonan, a vice president of Kidder, Peabody & Co., Inc., a New York investment banking firm that has underwritten issues under the program: "There is not much awareness of the program among companies. Additionally, in order to receive such financing, a sponsoring bank must map out details, and lots of banks aren't interested" ["Small Firms Aided in Pollution Financing," 1978, pp. 131-2].

The SEC is also making an effort to assist small businesses in raising capital. They have created a new Small Business Office which will:

1. develop and monitor rules designed to ease capital formation;
2. act as a liaison between small businesses and groups interested in their problems; and
3. deal directly with small businesses.

They have developed an alternative registration exemption for private placements and have reduced disclosure requirements for small business [Financial Reporting Briefs, p. 4].

Another effective way to make capital available to businesses would be to allow them to keep more of what they make by granting federal income tax relief. Indexing tax brackets to allow for inflation increases would be one way. Allowing companies to calculate depreciation on the current cost of productive assets (machinery, buildings, etc.) would be another. A third way would be to follow the recommendations of the report of the National Chamber's Center for Small Business. It recommended that specific steps should include:
Liberalize depreciation provisions.

• Make the investment tax credit permanent and raise the limit on used equipment to $200,000.

• Expand the capital gains deduction and reduce the tax rate on capital gains proportionate to the length of time a capital asset is held.

• Increase the minimum accumulated earnings credit to $500,000.

• Allow a net operating loss carry-back of three years and a carry-forward of eight years.

• Permit a deferral of the tax on the sale of equity in a small business if proceeds are reinvested in other small businesses.

• Refund overpayments of estimated income tax when claimed, rather than at year end.

• Double the current limits on special treatment of capital losses on small business in investments under Section 1244 of the Internal Revenue Code.

• Retain present deductions for non-business interest.

• Increase the corporate surtax exemption to $200,000 and reduce the normal tax rate on the first $50,000 of income.

• Reduce rates on corporate and individual income generally

[Improving the State of Small Business, 1978, p. 38].

The SBA also made some specific recommendations for tax relief for small businesses in its report entitled, The Study of Small Business. That report recommends the creation of a new taxpaying entity called a "Small Business Enterprise" (SBE), which would be entitled to certain tax advantages.

Interestingly, in England a questionnaire was sent to chairmen and managing directors of large British companies who were asked, "Do you agree that flourishing small and medium-sized businesses urgently need more encouragement if Britain is to stage a real economic recovery?" The over-all results were:

The general feeling was that the prime responsibility of government was to create the right environment for the foundation
and growth of small businesses. The priority, every director emphasized, was reform of the tax system, a lessening of the disincentive of high taxation on personal income and company profits. Next, there was a crying need to reduce bureaucracy and rescue the businessman from immersion in floods of paperwork... [Bull, 1977, pp. 60-1].

Other items. General economic forecasts seem to be numerous but very often inaccurate. The respondents to the questionnaire seemed to be indicating that they wanted accurate economic forecasts. This researcher will not presume to state how this can be accomplished.

A summary and interpretation of government regulations affecting small businesses may prove helpful. The information exists in individual documents. Possibly a combination and condensation of the information in clear language is what is being sought. Of course, if the amount of regulation could be reduced, this would contribute to the task.

Important Areas of Research

Ways to reduce government regulation of small businesses. This was identified as the most important area for research by respondents to the questionnaire. Barbara Hackman Franklin, Commissioner of the Consumer Product Safety Commission, summarized the issue in a recent article when she stated:

The sheer volume of governmental regulations -- state, local and federal -- add up to a cumulative burden which is particularly difficult for small businesses.

One regulation alone may not be unreasonable in terms of increased costs or decreased productivity for a small company. But when that same company must also absorb the effects of regulation from several other federal agencies, plus state and local agencies, the total burden can be its undoing. If too many companies fail and thus reduce competition, product safety, quality, price, and variety may also be adversely affected [Franklin, 1978, p. 54].
Ms. Franklin recommended the following concerning her own Commission to help reduce the regulatory burden:

- Take a closer look at precisely when safety regulation makes sense, under what circumstances, and to what extent. Where regulation is needed, we should make it better, make it work, and make it stick. In those cases where regulation isn't required, we should say so and act accordingly.

- Ensure that adequate cost-benefit analysis is done prior to regulatory action with a particular concern for the impact on small business.

- Consider exemptions and other appropriate measures to reduce the regulatory burden on small companies.

- Identify small business groups and individual companies which could be affected by particular regulations, and solicit their views at the earliest stages in the process. One way to do this is to schedule more regional hearings.

- Invite representatives of small businesses to meet with the commission or with individual commissioners to discuss their concerns before regulatory decisions are made. About a year ago, I began doing this and found it extremely helpful.

- Conduct educational seminars around the country to inform business about regulations that will be issued. Through June, the Consumer Product Safety Commission has conducted approximately 50 such seminars, attended by about 3,600 representatives, mostly from small businesses.

The commission is working on these steps to get the voice of small business into the decision-making process. I believe other regulatory agencies could take the same steps [Franklin, 1978, p. 55].

The cost of complying with government regulations was recently studied by Arthur Andersen & Co., one of the nation's largest public accounting firms. Its findings were as follows:

Regulations of only six federal agencies and programs cost the 48 corporations $2.6 billion in 1977. Harvey Kapnick, chairman of Arthur Andersen, pointed out that the cost was equivalent to an increase in the corporate tax rate to 55% from 48%.

The $2.6 billion incremental cost was equal to 43% of what the 48 companies spent on research and development and to 16% of net income.
The manufacturing sector was affected most heavily. Its $2.3 billion in incremental costs was equal to 23% of net income.

Our firm could not study all federal regulatory agencies within the scope of available resources. We chose six agencies and programs whose regulations affect a wide variety of industries. We studied the Environmental Protection Agency (EPS), Equal Employment Opportunity (EEO), Occupational Safety and Health Administration (OSHA), Department of Energy (DOE), Employee Retirement Income Security Act (ERISA) and the Federal Trade Commission (FTC) ["What Regulations Cost: Highlights of Business Roundtable Study," 1979, p. 3].

The study identified nine attributes of regulations which result in high incremental cost. They are:

1. Continuous monitoring is required.
2. New technology is required to meet compliance.
3. New equipment must be purchased.
4. Required actions lead to recurring costs.
5. Existing facilities must be modified.
7. Inadequate risk assessment is made of the stringent standard required.
8. The elimination of a hazardous substance or condition by engineering methods is required.
9. Requirements are subject to change ["What Regulations Cost: Highlights of Business Roundtable Study," 1979, p. 4].

A followup study is to be conducted by Arthur Andersen & Co. The new study will measure the direct incremental cost incurred by about 100 companies of various size in complying with the regulations of six federal agencies and programs in 1978. It will apply the concepts used in the first study to broader segments of the economy.
Efforts such as those undertaken by Arthur Andersen & Co. should be encouraged. Also further research should be conducted. When costs of complying with specific regulations are known, the task of reducing over-all costs can better be addressed.

The report of the National Chamber's Center for Small Business applauded some of the initiatives taken by the current administration in seeking to make the regulatory function more effective and less burdensome. The report urged:

that regulatory reform efforts be based on maintenance of a competitive free market system as the primary source of meeting consumer needs, with regulation only to the extent essential to protect health, safety, and the general welfare. Regulation, the report says, should be administered so as to eliminate uneven and inequitable enforcement as well as duplication or conflict in requirements.

Procedures, it says, should provide for prompt regulatory decisions consistent with due process, should ensure adequate consideration of costs and benefits, and should minimize compliance costs [Improving the State of Small Business, 1978, p. 41].

The report also urged that recommendations made by the Commission on Federal Paperwork be implemented as soon as possible so as to decrease the cost of preparing paperwork required by regulatory agencies.

Ways to simplify the federal income tax law. Each time an attempt is made to simplify the tax law, the result is labeled "the full employment act for accountants and lawyers." The law seems to become more and more complicated with time. Possibly we are trying to accomplish too many social and other goals through our tax law. The complexity of the regulations forces the businessman to hire an expert to prepare business and personal tax returns. Possibly the government should fund research projects directed toward making the computation of the amount of tax due simple enough so that most businessmen and individuals could prepare their own returns.
Ways to reduce the cost of borrowing for small business. This topic has been addressed earlier in this report. A search for new methods for reducing the cost of capital for small businesses should be encouraged. Many persons believe the profit squeeze created by having to invest greater and greater amounts in inventory and receivables is due at least in part to inflation. The sources of capital available to small businesses are very limited and may become even more limited in the future.

The effect on small business of increasing the minimum wage. Raising the minimum wage sounds like a "God, motherhood and apple pie" issue. Who could possibly oppose it? It is designed to raise the wages of workers who earn very low wages so that they may have a decent standard of living. It actually accomplishes this for those who remain employed after the increase. But it causes others to be terminated because their value is less than the wage they must be paid. Many of these workers end up drawing unemployment checks. Thus, many of those whom the increase is designed to benefit actually become its victims.

There is also an increased cost to small business which results from increasing the minimum wage. It contributes to the hopeless feeling that many of those who are in small business have when faced by one cost increase after another. A quote from a recent article illustrates this feeling:

Leonard Schneider, president of Schneider Hardware, a three-store home center chain in Pittsburgh, PA, sees the new minimum wage law as a threat to retailers and consumers alike.

"It is going to mean an increase of at least 10% in our payroll. I'll have to do a price mark-up of 5% just to cover the payroll increase -- and that's just in the first year," he said.

"It's tough enough now to make a living," Schneider said. "I can't imagine what it's going to be like in a few years" [Butler, 1978, p. 18].
5. THE BIG PICTURE

Small business, along with the rest of the United States, is facing one of the most challenging periods in its history. Since 1973 we have been in an economic situation called stagflation. The information needs and important topics for research identified by respondents to the questionnaire can be discussed in terms of the stagflation situation we face. Much of the anger expressed by respondents can be related to this situation. Respondents face inflation, possible shortages of energy resources, high costs of operating, and the prospect of joining the ranks of the unemployed should their businesses fail.

If we can understand the current economic situation we are better able to do something about it. In past periods we have had to combat either inflation or unemployment. Under stagflation we have to combat both of them simultaneously. What causes this strange situation? Why don't the economic policies we have followed in the past seem to get us out of this situation? What do we need to do to get back to full employment at a reasonable price level for goods and services? Answering these questions would show us the way to lessen the magnitude of some of the problems faced by small businesses in the Southeast and throughout the United States. Before answering these questions we must digress for a moment.

The Keynesian Era

First we must review some background information regarding our economic history. From 1929 to 1940 the economic problem facing the United States was one of depression. It was brought about by a decrease in the quantity of goods and services demanded at each level of prices. This is shown in
Figure 1 as a shift of aggregate demand from AD to AD'. (Figure 1 is quite simple to understand. It shows the total demand and supply function (curves) for goods and services at each price level which is possible.) This shift in demand caused aggregate demand to intersect the aggregate supply curve at a different point and thus caused the price level to decline from OP_f to OP_d and the quantity of goods and services to decrease from OQ_f to OQ_d. The reduction in the quantity of goods and services provided in the economy led to a reduction in employment. In fact, the stereotype of people having to resort to selling apples and pencils on street corners to earn a living became reality for many.

In 1935, John Maynard Keynes, a fellow of King's College, Cambridge, England, wrote a book entitled The General Theory of Employment Interest and Money [Keynes, 1935]. The book taught us that the way out of a depression was to use fiscal and monetary policy to do so. Specifically, we could cut taxes, increase government spending, lower the interest rate, and increase the supply of money. These actions would shift aggregate demand to the right from AD' to AD. This shift caused output to increase to full employment output (OQ_f) and the price level to increase to OP_f.

Some would argue that the advent of World War II pulled us out of the depression. The massive increase in government spending was consistent with the Keynesian solution to the problem. In fact, inflationary pressures developed for consumer goods. People had rising incomes, but shortages developed since much of the productive capacity was directed to the production of war related goods rather than consumer goods. The only way to allocate the scarce consumer goods was to ration them. To purchase these goods you not only needed cash but also the proper rationing stamps. Price controls
Figure 1
The Economic Problem During Depression

Where:

\( \text{AS} \) = Aggregate supply of all goods and services in the United States

\( \text{AD} \) = Aggregate demand of all goods and services in the United States

\( OQ_f \) = Output which results in full employment

\( OP_f \) = Price level at full employment

were also in effect. Thus, government interfered with the free market system to prevent run-away inflation for consumer goods.

After the war, the pent-up demand for consumer goods still existed and we faced a period of inflation (depicted in Figure 2). High personal income levels and pent-up demand for goods and services (one could again buy automobiles, refrigerators, and washing machines) shifted aggregate demand to the right from \( \text{AD} \) to \( \text{AD}' \). As a result, the price level increased from its ideal position \( OP_f \) to \( OP_i \) and output increased from the full employment
level (OQ_f) to OQ_i (by people working overtime or two jobs). Again, Keynes' ideas were relevant to the problem. One only needed to take the reverse actions of those which had been taken to get us out of the depression. Specifically, we could raise taxes, cut government spending, raise the interest rate, and decrease the supply of money. These actions would shift the aggregate demand curve back to its proper position AD.

The actions recommended by Keynes could be used to "fine tune" the economy throughout the period of 1935 to 1973. We at times had some difficulty with this approach in that we stimulated or cooled off the economy too much, but the approach worked fairly well. Keynes seemed to have indeed written the general history which applied to any economy situation we faced. When unemployment increased we simply stimulated the economy by increasing demand. When inflation became the problem we merely dampened demand through fiscal and monetary policy.
All during this period the aggregate supply curve (AS) did not shift very much. To understand why, we must realize that this curve is the aggregate of all marginal cost curves faced by individual companies. It remained fairly stable because the cost of factors of production, especially energy, remained fairly stable. (While the cost of labor did increase, companies compensated for higher labor costs to a certain extent by automating production processes.)

**Stagflation**

In 1973 a dramatic outside element was introduced. The Arab nations increased oil prices by about four times the previous price. Since many of our production processes utilize oil or oil derived products, production costs increased substantially. This caused the aggregate supply curve to shift to the left from AS to AS' as shown in Figure 3. What this shift meant was that, because of higher costs faced by firms, they were willing to supply less goods and services at each possible price level.

This shift caused prices to increase from $O_P^f$ to $O_P^s$ and output to decline from $O_Q^f$ to $O_Q^s$. Notice that the price level went up even though output declined (and unemployment went up). We now were faced with not fighting either inflation or unemployment but both at the same time.

Those who view the economy through "Keynesian eyes" had difficulty in deciding what to do because the Keynesian solutions for inflation and unemployment are exactly the opposite. President Ford decided to concentrate on inflation through his WIN (whip inflation now) campaign, but mounting unemployment soon made him back away from restrictive fiscal and monetary policies. President Carter came into office and announced in his first and
second State of the Union messages that he would concentrate on lowering the unemployment rate. Attempts to do so worsened the inflation rate to the extent that he then shifted the emphasis in his third State of the Union address to fighting inflation through wage and price guidelines.

The ineffectiveness of Keynesian solutions to the current situation leads one to question whether his "general theory" was not really a "special theory" which applies only when the aggregate supply curve remains in a relatively constant position. Keynes undoubtedly saw the implications of a shifting supply curve, but did not concentrate on it because it was not a problem at the time he wrote his book.

The Solution to Stagflation

Unfortunately for us the aggregate supply curve is much more difficult to manipulate than is the aggregate demand curve, but we must try. If we
could only shift aggregate supply to the right from AS' to AS (in Figure 3) we would lower the price level and increase employment. Possible ways of doing this include many of the suggestions that respondents to the questionnaire would have the federal government do:

1. Reduce government regulation so as to reduce the costs it creates for businesses.
2. Simplify Federal income tax law (and possibly reduce the amount of taxes due) to lessen the cost incurred by business.
3. Find additional and less expensive sources of debt and equity capital.
4. Hold down labor costs by holding down the minimum wage.
5. Find means of increasing productivity.
6. Find ways to conserve energy (and/or find new cheap sources).

Any one or all of these would tend to shift aggregate supply back out to the right. This would occur because firms would be willing to supply more goods and services at each level of prices as a result of their own cost reductions. Some middle ground must be struck between the public interest as represented by regulation of business activities and public interest as represented by a strong and favorable business climate, lower prices, and more jobs. We must continually look for ways to reduce the cost of doing business. This could become an area of focus in federal grant programs and by business in general.

Now that we understand our new economic situation it is time to begin dealing with it by lowering factor costs, cutting government regulation, and increasing productivity so that small business can flourish in the United States. This is what those engaged in small business in the Southeastern United States seem to be requesting.
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THE STATUS AND OPPORTUNITIES OF SMALL BUSINESS IN FOREIGN TRADE IN REGION FOUR

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Florida International University

Arun Prakash, Assistant Professor
Florida International University

1. INTRODUCTION

This paper focuses upon the export behavior of small manufacturing firms in the following states: Alabama, Florida, Georgia, Kentucky, Mississippi, North Carolina, South Carolina and Tennessee (designated as S.B.A. Region Four). An analysis of the current status of export trade in the region is reported and the vehicles for expansion of export trade is assessed. In addition, recommendations are made concerning government policy felt necessary to expand export trade among small manufacturers in the region.

Data have been gathered from primary sources through the administration of survey questionnaires and through personal interviews. Secondary data have been obtained from sources published by the United States Department of Commerce. Also, some of the conclusions drawn here have been obtained from a survey of the current literature concerning small business international trade activities in the region.

Table 1 presents aggregate manufacturing export data for the individual states in the region. In 1976, aggregate manufacturing production in the region was $172.9 million. Of this amount $9.8 million, or approximately 5.7 percent, was exported. Total manufacturing employment in the region was approximately 3.2 million. Primary employment due to manufacutring for export totaled 143 thousand while induced or secondary employment was 135
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<tbody>
<tr>
<td>Alabama</td>
<td>330</td>
<td>13</td>
<td>18</td>
<td>$832</td>
<td>$17,988</td>
<td>5.6%</td>
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<td>332</td>
<td>20</td>
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<td>1,363</td>
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<td>469</td>
<td>21</td>
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<td>28,391</td>
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<tr>
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<td>277</td>
<td>12</td>
<td>12</td>
<td>1,137</td>
<td>20,268</td>
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<td>34</td>
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<tr>
<td>Mississippi</td>
<td>193</td>
<td>10</td>
<td>7</td>
<td>698</td>
<td>10,868</td>
<td>6.4%</td>
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<tr>
<td>North Carolina</td>
<td>739</td>
<td>32</td>
<td>30</td>
<td>2,202</td>
<td>35,891</td>
<td>6.1%</td>
<td>27</td>
</tr>
<tr>
<td>South Carolina</td>
<td>371</td>
<td>16</td>
<td>17</td>
<td>935</td>
<td>16,610</td>
<td>5.6%</td>
<td>35</td>
</tr>
<tr>
<td>Tennessee</td>
<td>479</td>
<td>19</td>
<td>19</td>
<td>1,253</td>
<td>24,756</td>
<td>5.1%</td>
<td>38</td>
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<td>TOTALS</td>
<td>3,190</td>
<td>143</td>
<td>135</td>
<td>$9,784</td>
<td>$172,863</td>
<td>5.7%*</td>
<td></td>
</tr>
</tbody>
</table>

*Average percent of total production exported

Source: U.S. Department of Commerce Industry and Trade Administration
thousand for an estimated total of 278 thousand. This represents approximately 8.7 percent of the total level of manufacturing employment in the region in 1976.

The last two columns of Table 1 give an indication of the extent of export effort in the region. The ratio of manufacturing exports to total manufacturing sales has been computed and each state has been numerically ranked according to the ratio. Note that only Florida and Mississippi rank above the national median rank of 25.5. Mississippi's ranking above the national median rank is somewhat misleading. The relatively high rank is the result of a low absolute level of manufacturing activity in the state (less than eleven billion dollars) rather than a high level of export intensity. Thus, on the whole there appears to be a general lack of export effort in the region.

Given the region's proximity to the Circumcaribbean Basin, the abundance of states with access to deepwater ports and access to international air terminals, this lack of export effort is surprising.

Table 2 indicates the ten-year growth pattern of manufacturing export sales for each state in the region. Over the period, the region has accounted for between nine and twelve percent of the nation's manufacturing export sales. The overall annual compound growth rate of the region's exports amounted to 15.2 percent and approximated the national growth rate of manufacturing exports. While on the surface the growth rate appears to be dramatic, it is somewhat misleading since data are given in nominal dollars. The growth rate in real terms over this inflationary period has been less than eight percent annually. Given the region's low level of manufacturing exports in 1966 (approximately $2.3 billion) and the fact that between 1966 and 1976 numerous midwestern and eastern manufacturers (who were already exporting a portion of their production) migrated to the region, the rate of growth indicates that there has been little transformation from domestic sales to
Table 2
Manufacturing Export Growth 1966-1976

<table>
<thead>
<tr>
<th>Export Value (millions $)</th>
<th>Annual Compound growth rate</th>
</tr>
</thead>
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<tr>
<th></th>
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<tbody>
<tr>
<td>Alabama</td>
<td>$186</td>
<td>$318</td>
<td>$287</td>
<td>$832</td>
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<tr>
<td>Florida</td>
<td>310</td>
<td>426</td>
<td>567</td>
<td>1,363</td>
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<tr>
<td>Georgia</td>
<td>354</td>
<td>428</td>
<td>580</td>
<td>1,364</td>
</tr>
<tr>
<td>Kentucky</td>
<td>300</td>
<td>345</td>
<td>451</td>
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<tr>
<td>Mississippi</td>
<td>137</td>
<td>181</td>
<td>236</td>
<td>698</td>
</tr>
<tr>
<td>North Carolina</td>
<td>560</td>
<td>739</td>
<td>705</td>
<td>2,202</td>
</tr>
<tr>
<td>South Carolina</td>
<td>180</td>
<td>254</td>
<td>312</td>
<td>935</td>
</tr>
<tr>
<td>Tennessee</td>
<td>340</td>
<td>472</td>
<td>679</td>
<td>1,253</td>
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</table>

<table>
<thead>
<tr>
<th>Totals</th>
<th>$2,367</th>
<th>$3,163</th>
<th>$3,817</th>
<th>$9,784</th>
</tr>
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<tbody>
<tr>
<td>U.S. Totals</td>
<td>$21,299</td>
<td>29,210</td>
<td>36,608</td>
<td>83,098</td>
</tr>
</tbody>
</table>

| Regions as % of U.S. | 11.1% | 10.7% | 9.1% | 11.7% |

Source: U.S. Department of Commerce Industry and Trade Administration
import sales in the region.

Reasons for the apparent lack of export expansion by small manufacturers in the region will be examined in the following sections of the paper. The next section of the paper focuses on small manufacturer's export behavior, the third section examines the current state of international banking activities in the region, the fourth section examines the status of international business education in the region. Finally, conclusions are drawn and policy recommendations are made in the last section.

2. SMALL MANUFACTURER'S MOTIVATIONS TO EXPORT

While nearly every one of the Fortune 500 Industrial Companies engages in foreign trade, it has been estimated that less than one of eight small businessmen (and perhaps a lesser amount in region four) export their products. This statistic has been viewed with great surprise by various state and federal government agencies. However, when one considers the objectives of the owners of small businesses and their motivations for operating their own businesses, the statistic is not so startling. Most small business entrepreneurs do not cite maximization of wealth as their single most important objective. The traditional view of the firm as a wealth maximizer, which is quite appropriate for the large corporation whose shares of stock are publicly held, may not hold true for a great many small entrepreneurs. Thus, even though there may exist profitable opportunities from the initiation of export sales (given the risk in such activities) small businessmen may not be significantly motivated to take advantage of them. Such businessmen are often quite content with wealth and profit "satisficing" rather than "optimizing" as long as the other business objectives (freedom, self satisfaction, achievement, etc.) are met. As a consequence, merely pointing out the beneficial risk-reward structure of international trade by various agencies may do little (and in fact does little) to motivate the small businessman to export.
These observations are underscored by the fact that of the small businessmen surveyed, many indicated that the decision to export was not part of the strategic plan of the firm. Most export activities were initiated by chance stimuli: unsolicited orders from a foreign customer or contacts made by domestic businessmen while vacationing in a foreign country. In addition, many businessmen who have considered exporting but have chosen not to do so found themselves educationally unequipped to undertake the project of organizing for export sales. Many felt that the export process and the associated agencies and regulations were bewildering. Others reported a lack of adequate foreign market information, a lack of resources (especially export personnel) and increased risk exposure of international transactions as reasons for not exporting their products.

The evidence as to why some firms specifically chose to export while others do not is somewhat clouded. As in previous research, personal interviews with manufacturers in the region were conducted to determine whether factors internal to the firm (e.g., excess capacity, domestic competition, profit motivation, etc.) or factors external to the firm (e.g., trade mission activities, trade fairs, U.S. Department of Commerce activity, SBA activity, sales agent activity, unsolicited orders or inquiries from foreign customers) were dominant motivators of export activity. Of the factors internal to the firm, profit motivation (and associated risk-reward perceptions of exporting) stood out as a significant factor. That is, of the firms surveyed, exporters appeared to possess higher profit expectation and lower risk perceptions from exporting than did non-exporters. This was true for those manufacturers of similar products located in the same geographical region. Of the factors external to the firm, the significant motivator to export was the unsolicited order or inquiry. More exporting firms responded that they had initially acquired unsolicited orders than non-exporting firms. However,
several non-exporting firms responded that they had received unsolicited orders from foreigners but had chosen not to export. Also, it was found that relative to non-exporters, exporters possessed higher levels of formal education and had participated more frequently in foreign travel than non-exporters. Additionally, for businessmen in the region (especially in Florida) those with foreign background (those born in foreign countries or those who had lived in foreign countries) were more likely to export than those with primarily domestic backgrounds. Thus, manufacturers in the region may be described as either "cosmopolitan" or "local." Those entrepreneurs who possessed international "mentalities" (cosmopolitans) appear more likely to engage in export activities than those without this mentality (locals). This finding is not surprising. However, it was surprising to find that of the many organized activities external to the firm (U.S. Dept. of Commerce, SBA, College and University Outreach programs, etc.) none appear to be significant motivators of export trade. This is probably true since attendance at these organized events is motivated by the existence of current problems which have resulted from exporting and a desire to obtain the experience of others who are participating in exporting. Thus, state and federal government agencies which offer export conferences and seminars may assist in the expansion of export trade by firms currently exporting but do not make significant contributions to the imitation of export activities by non-exporters.

3. INTERNATIONAL BANKING AND EXPORT STIMULATION

One of the prime requisites of international trade expansion is the existence of a viable banking structure which is willing and able to facilitate and finance international transactions. As pointed out earlier, international financial transactions, letters of credit, acceptances, credit analysis, etc. are often an area of confusion for the small businessman who is contemplating
exportsales. Thus, in addition to financing international trade, regional banks can perform important educational services to the small businessman.

A survey of banks in the region indicates that only approximately forty-five commercial banks possess active international departments. Of these banks about three-fourths offer complete international banking services. The remaining banks with active international departments have chosen to engage exclusively in trade financing activities. Most regional banks have chosen to direct trade financing and other international activities to their money center correspondent banks.

The banks in the region which operate international trade departments are located in the major cities in the region (i.e., Miami, Jacksonville, Atlanta, Mobile and Birmingham). Thus, the sparcity of regional banks with active international departments and the location of these departments greatly impedes the entry of the small domestic manufacturer in international trade. While it is true that international departments sell their international services to a much wider geographical area than their domestic services, few banks possess sufficient personnel to promote exporting to the non-exporter. Thus, most of the sales efforts of the regional international banking departments are aimed at current customers.

Of the banks with active international departments, nineteen indicated that they have chosen to concentrate their activities on a particular geographic region, especially the Circumcaribbean basin. This is not surprising given the proximity to Latin America, the transportation ties and the Latin business orientation in Florida. However, these numbers indicate a general lack of international expertise in and orientation toward lucrative markets in Europe and Asia. Thus, even for a highly motivated small businessman establishment of an international banking relationship with a regional bank may require extensive search and effort. The cost of search (in both time and money) may
inhibit the development of international trade activities by small businesses. In fact, the current state of international banking within the region inhibits rather than fosters the development of international trade.

At present, there may be little that can be accomplished by policy makers to stimulate international banking within the region. As more bankers realize the profit potential in international transactions more banks will develop active international departments and thus through aggressive competitive efforts seek out potential exporters and, hence, stimulate the growth of export sales. However, the current indication of bankers in the region is that the expansion of international activities will require numerous individuals with international financial expertise. These same bankers feel that currently the availability of these personnel is severely limited. This point is underscored by the fact that only eight universities in the region offer degree programs in international business and none offer area specializations in international banking. This sparcity of degree programs is not indigenous to the region but rather reflects the state of international business education nationally. Thus, it appears that it may be several years in the future before the region's banking community will possess sufficient international banking services to actively promote international trade. It is envisioned that in the interim regional banks will only play a passive role in international trade development.

4. INTERNATIONAL BUSINESS EDUCATION

This section assesses the role played by region colleges and universities as providers of support services to the small businessman interested in developing or expanding export activities. A questionnaire instrument was distributed to all schools who are members and affiliates of the AACSB in the region. Thirty-two colleges responded. Of these, thirty indicated that they
currently offer international business courses as part of their curriculum. However, only fifteen indicated course offerings in marketing and only twelve participated in international business seminars offered to local businessmen. In three states, Tennessee, Kentucky and Mississippi, no such seminars were offered. Thus, it appears that this valuable resource has been virtually untapped.

Of those institutions which offered seminars in exporting, most were conducted in cooperation with the United States Department of Commerce, SBA offices, and/or state international trade agencies. Respondents reported that these seminars were well attended. However, over the past year less than one thousand small business participated in these seminars in the region. These facts are quite startling. Colleges and universities have fallen quite short in the dissemination of export trade information to the small business community. Rather than assuming a dominate leadership role in the promotion of international trade, these institutions have played a passive role. That is, they have often acted as host for programs presented by other agencies rather than initiating the programs.

Many respondents indicated a willingness to develop programs in international business but indicated that they have been unable to obtain sufficient funds for the staffing and promotion of both academic and outreach programs. Thus, it is recommended that funding be made available through grant programs administered both to the Small Business Administration and the United States Department of Commerce. Seed grants should be established and active promotion by relevant government agencies can be utilized to establish outreach centers at regional colleges and universities. Such centers could be coordinated by international business faculty. The purpose of the centers would be twofold: (1) to stimulate and promote exporting by local businessmen and (2) to coordinate local international business education efforts. In
this way, greater use of this valuable source can be obtained.

5. CONCLUSIONS AND RECOMMENDATIONS

The region generally suffers from a lack of export activity by small manufacturers. Less than fifteen percent of the small manufacturers in the region export a portion of their production. This number represents only one-half of the region's small manufacturers which could successfully export their products. Of the reasons for export development commonly given by theoreticians (growth, keeping pace with domestic competitors, following domestic customers who have gone abroad, earn additional income on existing technology, spread fixed costs over larger sales volume, and competing with foreign companies that have involved domestic markets), none were found to be significant motivators of export trade among the small manufacturers studied. The greatest single motivator was found to be the unsolicited order from abroad. However, many non-exporters did not respond positively to this stimulus. Other external stimuli (government agencies, trade fairs, etc.) were also found to be insignificant motivators of export trade.

Some small manufacturers have international mentalities and others do not. Those who possess international backgrounds are much more inclined to export their products than those without such backgrounds. Further, attempts to educate businessmen and thus promote international business awareness have been relatively unsuccessful. Most educational programs were attended by current exporters interested in expansion of current export sales or in solving problems created by existing export activities. The U.S. Department of Commerce, the Small Business Administration, the regional banking system, and the region's colleges and universities were all equally unsuccessful in stimulating international business awareness. Overall, the lack of international economic infrastructure and (except for South Florida)
the absence of international mentalities among businessmen has inhibited
the growth of export trade with the region.

We feel that the greatest gains towards meeting the region's export
potential can be made by the systematic introduction and maintenance of an
international business education program. This program would be coordinated
by regional colleges and universities and would be funded by both state and
federal grants. The program would consist of both classroom education and
on-site assistance. Classroom activities would include both the lecture
approach and the experiential approach. Local exporters could be called upon
to share their export experiences. In the case of on-site education
activities, the small manufacturer could be taken step by step through the
export process using the manufacturer's current product line. This is
especially appealing in the case where the manufacturer has obtained an
unsolicited order from a foreign customer. Further, government subsidies
should be provided to assist the small manufacturer in filling the first
foreign order. Finally, technological assistance would be provided by
faculty members at participating institutions. Both regional offices of the
U.S. Department of Commerce and the Small Business Administration would be
encouraged to participate in the export development programs. We feel that
only through such a concerted effort will inroads be made toward motivating
the small manufacturer to export.
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U.S. Department of Commerce, Exports: State Export Series, Industry and
THE IMPORTANCE OF SMALL BUSINESS IN RURAL DEVELOPMENT OF THE REGION

G. Donald Jud
University of North Carolina

1. INTRODUCTION

The nonmetropolitan South traditionally has been a region of poverty and economic stagnation. Income has been low and economic opportunities have been limited, causing large numbers of the region's population to move elsewhere. During the 1960s, for example, nonmetropolitan counties in the South lost about 717,000 persons from outmigration. Since 1970, however, the economic plight of nonmetropolitan areas in the South has changed dramatically. The Bureau of the Census estimates that nonmetropolitan counties in the South have gained more than 620,000 residents from immigration since 1970.

The recent renaissance of nonmetropolitan areas has occurred not only in the South but throughout the nation. A 1978 Rand Corporation report notes that since 1970 population growth has been most rapid in the least urbanized and more remote counties all across the country (McCarthy and Morrison, 1978). The report speculated that this new trend might mark the beginnings of an entirely new national settlement pattern in which advances in transportation and communication technology and the heightened desire for natural amenities compete to bring about the settlement of more and more people in places separated from large urban centers.
The resurgence of growth in rural areas has important implications for public-sector planners as well as private-sector entrepreneurs. From a planning standpoint, the recent growth of nonmetropolitan areas represents the realization of a goal long sought by advocates of rural development. Nonmetropolitan growth has the potential to improve the economic status of the poorer segments of the rural population while, at the same time, relieving some of the growth pressures on larger cities that many have feared would damage severely the quality of urban life. In the private sector, nonmetropolitan growth has created significant new opportunities for the development of small business in all sectors of the rural economy, and small business expansions have played a key role in the recent upsurge of activity in the nonmetropolitan economy.

This paper focuses on nonmetropolitan economic development in the SBA's eight-state southern region—Alabama, Florida, Georgia, Kentucky, Mississippi, North Carolina, and South Carolina, and Tennessee. The second section of the paper documents recent trends in the growth of the southern economy since 1970. The third section identifies the role that small business has played in regional growth and development. The final section discusses the implications of recent trends for small business assistance in the South.

2. RECENT GROWTH TRENDS

Population. Population in the United States increased 6.2 percent between 1970 and 1977, rising from 204 million to 216 million. During the same period, the rate of population growth recorded by each of the eight southern states was significantly above that recorded for the nation as a whole (Table 1). Population in metropolitan areas in the South increased 13 percent and the nonmetropolitan population 10 percent. In the nonmetropolitan sector, the population growth rate was above the national
Table 1
Population Growth in the South, 1970-77

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<td>Number</td>
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<td>Metropolitan</td>
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<td>1,333,000 (22.5)</td>
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<td>6,845,400</td>
<td>8,452,100</td>
<td>1,606,700 (23.5)</td>
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<td>146,000 (3.2)</td>
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<td>1,560,300</td>
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<td>108,200 (6.3)</td>
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<td>Total</td>
<td>3,230,600</td>
<td>3,458,500</td>
<td>227,900 (7.1)</td>
<td>73,300 (2.3)</td>
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<td>Metropolitan</td>
<td>545,200</td>
<td>636,400</td>
<td>91,200 (17.0)</td>
<td>41,400 (7.6)</td>
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<td>1,753,000</td>
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<td>Total</td>
<td>2,221,100</td>
<td>2,389,400</td>
<td>168,300 (8.0)</td>
<td>14,000 (.6)</td>
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<td>2,497,100</td>
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<td>71,900 (3.1)</td>
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<td>2,807,200</td>
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<td>220,800 (8.0)</td>
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<td>Total</td>
<td>5,099,200</td>
<td>5,525,100</td>
<td>425,900 (8.4)</td>
<td>144,600 (2.8)</td>
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<td>Metropolitan</td>
<td>1,228,200</td>
<td>1,383,100</td>
<td>154,900 (13.0)</td>
<td>67,700 (5.5)</td>
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<td>1,492,600</td>
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<td>Total</td>
<td>2,598,200</td>
<td>2,875,700</td>
<td>277,500 (11.0)</td>
<td>99,300 (3.8)</td>
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<td>2,170,700</td>
<td>207,600 (8.3)</td>
<td>75,800 (3.0)</td>
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<td>1,588,600</td>
<td>154,700 (11.0)</td>
<td>103,500 (7.2)</td>
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<td>Total</td>
<td>3,937,000</td>
<td>4,299,300</td>
<td>263,300 (9.2)</td>
<td>179,300 (4.6)</td>
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<td>Metropolitan</td>
<td>18,748,000</td>
<td>21,198,800</td>
<td>2,450,800 (13.0)</td>
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<td>14,539,300</td>
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<td>620,700 (4.7)</td>
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<td>Total</td>
<td>31,986,700</td>
<td>35,738,000</td>
<td>3,751,300 (12.0)</td>
<td>2,188,500 (6.8)</td>
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<td>Total</td>
<td>203,798,700</td>
<td>216,339,000</td>
<td>12,540,300 (6.2)</td>
<td>3,140,000 (1.5)</td>
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</table>

average in each of the eight southern states except Mississippi. In Florida, the rate of population growth was 30 percent in nonmetropolitan areas.

Since 1970, increasing numbers of people have moved from the nation's large northern metropolitan centers and into the Sunbelt, including the South and West. The Bureau of the Census estimated that, during the 1970-77 period, net migration (i.e., the difference between the number of people moving into and out of an area) into the South was almost 2.2 million. And of this total, 620,700 represented net migration into nonmetropolitan places in the South. Net migration was estimated at 108,200 in the nonmetropolitan areas of Kentucky and 103,200 in Tennessee. Only Mississippi of the eight southern states recorded a negative net migration in nonmetropolitan areas. In three of the southern states--Kentucky, North Carolina, and Tennessee--the estimates of net migration actually were higher for nonmetropolitan locales than for metropolitan areas.

When confronted with statistics indicating a resurgence of population growth in nonmetropolitan areas, most people are prone to be somewhat skeptical and to wonder if the figures might not simply indicate an increased rate of residential sprawl out of metropolitan areas into adjacent rural locales. This question has been examined at the national level and several recent studies have shown that significant population growth has occurred in counties not adjacent to metropolitan areas (Beale, 1975; McCarthy and Morrison, 1978). It is now well established that the recent growth of nonmetropolitan counties cannot be explained by the influence of metropolitan expansion: The correlation between net migration rates and metropolitan adjacency which was strong in the 1960s has now largely disappeared.
Employment. Another consistent finding that has surfaced in studies of nonmetropolitan growth since 1970 is the high correlation between population and employment growth. Population and employment have risen together in nonmetropolitan areas as more and more people have begun both to live and to work farther from urban places.

In the southern region, employment growth has been more rapid in nonmetropolitan areas than in the region's more urban locales (Table 2). During 1970-77, total employment increased 29.8 percent in nonmetropolitan areas and 25.1 percent in the region's metropolitan districts. In 1977, 44 percent of all nonagricultural employment in the region was in nonmetropolitan areas. In Kentucky, Mississippi, and South Carolina, the majority of total employment was in nonmetropolitan areas in 1977.

Nationally, total nonagricultural employment rose 16.3 percent between 1970 and 1977. A glance at Table 2 reveals that the rate of employment growth in each of the southern states exceeded the national average during this period in both metro and nonmetro areas. Nonmetropolitan employment growth in Florida recorded a dramatic 70.3 percent increase.

Personal Income. How has the pattern of growth affected the general level of economic well-being in the region? The most comprehensive measure of economic well-being that is available at the regional level is personal income per capita. Personal income is calculated as the sum of all income received by individuals before the payment of personal taxes. Dividing by population gives a measure of the average income of individuals (including men, women, and children) before taxes.

At the national level, per capita personal income rose 80.5 percent during 1970-77, rising from $3,893 in 1970 to $7,026 in 1977. At the same
Table 2
Nonagricultural Employment Growth in the South, 1970-77

<table>
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<tr>
<td></td>
<td>Number</td>
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<td>540,900</td>
<td>100,300</td>
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<td>2,040,600</td>
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<td>524,000</td>
<td>892,600</td>
<td>368,600</td>
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<td>2,933,200</td>
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<td>1,917,400</td>
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<td>505,400</td>
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<td>653,400</td>
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<td><strong>Mississippi</strong></td>
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<td>Total</td>
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<tr>
<td>Metropolitan</td>
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<td>184,810</td>
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<td>Total</td>
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<td>Total</td>
<td>69,469,000</td>
<td>80,768,000</td>
<td>11,299,000</td>
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Source: U.S. Department of Labor
time, the all-items consumer price index rose 56.1 percent nationally. An examination of Table 3 reveals that the rate of increase recorded in personal income per capita in the nonmetropolitan areas of the southern states was, in every case, more rapid than the growth of income growth for the nation as a whole. Overall, per capita personal income rose 91.6 percent in the nonmetropolitan areas of the South.

The rapid income gains recorded in nonmetropolitan areas indicate that economic growth has closed some of the gap between income levels in the nonmetropolitan South and elsewhere, but the differential in nominal income still remains quite large. In 1977, nonmetropolitan per capita income in the South was $5,035, or about 72 percent of the average for the nation. While a considerable fraction of this regional differential in income is attributable to the lower real wages paid to workers in the rural South, a not insignificant fraction of the nominal income gap also is due to regional differences in the cost of living. The relative importance of regional cost-of-living differences is difficult to access with precision and, as a result, has become a subject of debate among economists. However, living costs differences do explain a large portion of the North-South income gap. The significance of the cost-of-living differential has been clearly established in a recent article by Don Ballante (1979) that showed for the South as a whole in 1970, over 62 percent of the difference between southern and northern money incomes could be explained by differences in living costs. To correct for regional cost-of-living differences, Ballante suggested that southern money income figures in 1970 should be increased almost 14 percent. If this same kind of cost-of-living differential prevailed in 1977, per capita personal income in the nonmetropolitan South
Table 3
Personal and Per Capital Margin in the South, 1970-77

<table>
<thead>
<tr>
<th></th>
<th>Total Personal Income</th>
<th>Per Capita Personal Income</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Alabama</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>6,706,800</td>
<td>14,047,300</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>3,270,700</td>
<td>6,738,100</td>
</tr>
<tr>
<td>Total</td>
<td>9,975,500</td>
<td>20,785,400</td>
</tr>
<tr>
<td><strong>Florida</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>22,637,100</td>
<td>50,107,200</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>2,680,300</td>
<td>6,496,200</td>
</tr>
<tr>
<td>Total</td>
<td>25,317,300</td>
<td>56,603,300</td>
</tr>
<tr>
<td><strong>Georgia</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>9,856,500</td>
<td>19,556,200</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>5,341,400</td>
<td>10,742,300</td>
</tr>
<tr>
<td>Total</td>
<td>15,197,900</td>
<td>30,298,400</td>
</tr>
<tr>
<td><strong>Kentucky</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>5,620,800</td>
<td>11,097,600</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>4,316,600</td>
<td>9,615,300</td>
</tr>
<tr>
<td>Total</td>
<td>9,937,300</td>
<td>20,712,900</td>
</tr>
<tr>
<td><strong>Mississippi</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>1,720,600</td>
<td>3,818,700</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>3,936,200</td>
<td>8,192,700</td>
</tr>
<tr>
<td>Total</td>
<td>5,656,800</td>
<td>12,011,400</td>
</tr>
<tr>
<td><strong>North Carolina</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>8,347,700</td>
<td>16,590,800</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>7,969,400</td>
<td>16,096,100</td>
</tr>
<tr>
<td>Total</td>
<td>16,317,100</td>
<td>32,686,900</td>
</tr>
<tr>
<td><strong>South Carolina</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>3,982,300</td>
<td>8,501,700</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>3,686,000</td>
<td>7,714,500</td>
</tr>
<tr>
<td>Total</td>
<td>7,668,400</td>
<td>16,216,200</td>
</tr>
<tr>
<td><strong>Tennessee</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>8,540,300</td>
<td>17,325,500</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>3,580,200</td>
<td>7,614,900</td>
</tr>
<tr>
<td>Total</td>
<td>12,120,500</td>
<td>24,940,400</td>
</tr>
<tr>
<td><strong>Southern Region</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Metropolitan</td>
<td>67,412,100</td>
<td>141,045,000</td>
</tr>
<tr>
<td>Nonmetropolitan</td>
<td>34,780,800</td>
<td>73,210,100</td>
</tr>
<tr>
<td>Total</td>
<td>102,192,900</td>
<td>214,255,100</td>
</tr>
<tr>
<td><strong>United States</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>793,485,000</td>
<td>1,519,893,000</td>
</tr>
</tbody>
</table>

would be $5,740 ($5,035 \times 1.14), or 82 percent of the national average when measured in real terms.

**Structural Change.** In seeking to understand the factors motivating the recent changes in income, employment, and population in the rural South, it is interesting to inquire into the patterns of structural change in the region. Just what are the industries in the region that appear to be growing most rapidly? Nationally, there has been substantial growth in manufacturing employment in nonmetropolitan counties since the 1960s (Morrill, 1978). At the same time, manufacturing employment has declined both in relative and absolute terms in the nation's urban centers.

Table 4 shows the pattern of structural change in the southern economy since 1970. The South recorded increases in employment in every major sector of the nonagricultural economy in both metro and nonmetro areas. These gains were well above the increases recorded in the corresponding sectors nationally.

In every sector except government, the growth of employment since 1970 has been more rapid in the nonmetropolitan areas of the South than in the more urban areas. The rate of increase in manufacturing employment in the rural South has been almost three times as rapid as manufacturing growth in urban areas of the South. Between 1970 and 1977, 262,690 new jobs were added to the manufacturing sector in nonmetropolitan areas. In 1977, manufacturing employment in southern nonmetro areas totaled 1,902,870.

Impressive also are the large increases in employment recorded in services (50%), trade (42%), finance (41%), and construction (38%) in the nonmetropolitan South since 1970. This expansion in nonmanufacturing sectors suggests that nonmetro growth is severing some of the economic
Table 4

Nonagricultural Employment Growth by Industry in the South, 1970-77

<table>
<thead>
<tr>
<th>Industry</th>
<th>Metropolitan Areas</th>
<th>Nonmetropolitan Areas</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1970</td>
<td>1977</td>
</tr>
<tr>
<td>Construction</td>
<td>361,030</td>
<td>381,320</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1,428,420</td>
<td>1,508,330</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>408,470</td>
<td>464,310</td>
</tr>
<tr>
<td>Wholesale &amp; Retail Trade</td>
<td>1,329,600</td>
<td>1,742,170</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>330,660</td>
<td>440,320</td>
</tr>
<tr>
<td>Services</td>
<td>913,370</td>
<td>1,343,140</td>
</tr>
<tr>
<td>Government</td>
<td>997,090</td>
<td>1,336,360</td>
</tr>
<tr>
<td>Total</td>
<td>5,768,640</td>
<td>7,215,950</td>
</tr>
<tr>
<td></td>
<td>228,970</td>
<td>314,780</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>1,640,180</td>
<td>1,902,870</td>
</tr>
<tr>
<td>Transportation &amp; Public Utilities</td>
<td>193,730</td>
<td>233,390</td>
</tr>
<tr>
<td>Wholesale &amp; Retail Trade</td>
<td>771,600</td>
<td>1,098,430</td>
</tr>
<tr>
<td>Finance, Insurance &amp; Real Estate</td>
<td>134,640</td>
<td>190,080</td>
</tr>
<tr>
<td>Services</td>
<td>561,830</td>
<td>842,560</td>
</tr>
<tr>
<td>Government</td>
<td>851,410</td>
<td>1,107,540</td>
</tr>
<tr>
<td>Total</td>
<td>4,382,360</td>
<td>5,689,650</td>
</tr>
</tbody>
</table>

Total Employment                  | 10,151,000         | 12,905,600            | 27.1     |

Source: U.S. Department of Labor.
ties that in the past have drawn economic activity into the urban centers. As more and more people have decided to live and work away from the urban cores of the region, many economic activities (such as retail trade, various types of services, etc.) that may once have been available only in urban areas are beginning to be available in more rural settings. These changes appear to augur for the creation of significant new opportunities for small business development in smaller communities throughout the South as rural entrepreneurs begin to confront an expanding horizon of profit opportunities.

3. THE ROLE OF SMALL BUSINESS

Is it possible to infer anything about the performance of small business in the nonmetropolitan South on the basis of recent trends in regional growth? Or, stated another way, how much of the region's improved economic performance is attributable to the growth of small business? In order to answer this question, one must first provide an acceptable definition of small business. The SBA has suggested that small business includes all firms with less than 500 employees. Others have suggested that 20 employees be used as the dividing line.

Table 5 shows the percent of total employment in each major industrial sector in the South accounted for by small business, using the SBA definition of less than 500 employees. A striking finding evident from Table 5 is that more than 50 percent of all employment in nonagricultural sectors in the South is in establishments of less than 500 employees. This is true even in the manufacturing sector. In the trade and services sectors, the percentage of small business employment ranges from 80 to 90 percent. If we assume that the relative importance of small business does not vary significantly between southern metro and nonmetro areas, Table 5 suggests that the great majority of employment growth in the nonmetropolitan South has resulted from expansion by small businesses.
Table 5

Percent of Employment in Small Business in the South, 1976

<table>
<thead>
<tr>
<th></th>
<th>Alabama</th>
<th>Florida</th>
<th>Georgia</th>
<th>Kentucky</th>
<th>Mississippi</th>
<th>North Carolina</th>
<th>South Carolina</th>
<th>Tennessee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>48%+</td>
<td>72%</td>
<td>100%</td>
<td>100%</td>
<td>40%</td>
<td>100%</td>
<td>52%+</td>
<td>100%</td>
</tr>
<tr>
<td>Mining</td>
<td>82</td>
<td>61+</td>
<td>24</td>
<td>87</td>
<td>100</td>
<td>94+</td>
<td>100</td>
<td>59+</td>
</tr>
<tr>
<td>Construction</td>
<td>89</td>
<td>96</td>
<td>92+</td>
<td>95+</td>
<td>89+</td>
<td>92</td>
<td>59+</td>
<td>92+</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>61</td>
<td>71</td>
<td>64</td>
<td>57</td>
<td>61</td>
<td>61</td>
<td>51</td>
<td>58</td>
</tr>
<tr>
<td>Transportation</td>
<td>75</td>
<td>69</td>
<td>58</td>
<td>92+</td>
<td>90+</td>
<td>63</td>
<td>89+</td>
<td>80</td>
</tr>
<tr>
<td>Wholesale</td>
<td>94+</td>
<td>96+</td>
<td>98</td>
<td>96+</td>
<td>100</td>
<td>93+</td>
<td>100</td>
<td>97</td>
</tr>
<tr>
<td>Retail</td>
<td>98</td>
<td>96</td>
<td>93</td>
<td>99+</td>
<td>96+</td>
<td>97</td>
<td>98</td>
<td>96</td>
</tr>
<tr>
<td>Finance</td>
<td>88</td>
<td>89</td>
<td>87</td>
<td>91+</td>
<td>67+</td>
<td>85</td>
<td>69+</td>
<td>86</td>
</tr>
<tr>
<td>Services</td>
<td>87</td>
<td>82</td>
<td>87</td>
<td>86</td>
<td>82+</td>
<td>85</td>
<td>89</td>
<td>79</td>
</tr>
</tbody>
</table>

+ Indicates that the actual percentage is larger than the number shown.

Source: U.S. Department of Commerce, Bureau of the Census, County Business Patterns, 1976. Percentages calculated from Table 1C.
One failing of Table 5 is that it is based on employment data classified by establishment size rather than by size of the total enterprise. Branch plants are treated as separate establishments even though they may form a part of one large national or multinational enterprise. Fortunately, additional evidence on the importance of small business is available from some recent research by David Birch (1979).

Professor Birch, working with a grant from the Economic Development Administration, has developed a data file on the employment histories of 5.6 million business establishments. Together, these 5.6 million firms account for about 82 percent of all private sector employment. Tabulations from this file suggest that almost all of the new employment in the U.S., regardless of the specific region examined, is the result of the birth of new firms or the expansion of old establishments. Virtually no firms migrate from one region to another, and even though branch plants may be opened in a new region, the operation of the branch hardly ever results in the complete loss of employment in the parent facility. Birch's findings suggest that employment growth in the nonmetropolitan South cannot be attributed to the wholesale movement of firms out of other regions, as if often reported to have occurred with the migration of textile firms out of New England and into the South in the years following World War II.

Much more remarkable, however, are Birch's findings regarding the role of small enterprise in the job-creation process. On the basis of his sample of firms, it appears that 42.7 percent of all new jobs in the South between 1960 and 1976 were created through the birth or expansion of small, independent enterprises with less than 20 employees. Nationally, such small businesses accounted for 51.8 percent of all new jobs, calculated on the basis of his survey.
When Birch stratified his sample by age of establishment, he uncovered another very interesting statistic: Almost 80 percent of all new jobs created during 1974-76 were in establishments less than 4 years old. This average percentage was somewhat lower in manufacturing and higher in trade and services, but it tended to be very stable across major regions of the country.

Overall, Birch's research suggests that much of the employment growth that has occurred in the nonmetropolitan South has resulted from the birth and expansion decisions of small, young, independent firms. Available data and research indicate that small businesses are active in all sectors of the rural southern economy, and represent a significant factor fostering the creation of new jobs in the region. Indeed, the continued economic health of the region depends on the maintenance of an economic environment that is contributive to the growth and expansion of small business enterprises.

4. IMPLICATIONS FOR SMALL BUSINESS ASSISTANCE

It is clear from the foregoing that the focus of growth is shifting outward from urban areas in the South to more rural locales. Exactly why this shift is occurring is not known precisely, but current research suggests not only the importance of cost factors but also a heightened desire on the part of individuals, managers, and entrepreneurs for the natural amenities of more outlying areas. The major advances in transportation and communications technology together with the massive investments in infrastructure that occurred following World War II were necessary preconditions if not also direct contributing factors to this process.
Throughout the South, growth is spreading to those areas which seem most able to accommodate it and most in need of the positive benefits that it generates. The growth that has occurred in the nonmetropolitan South has had discernible positive effects on the economic well-being of the rural population, and even though a significant differential remains between average incomes in the nonmetropolitan South and elsewhere, economic growth has begun to close the gap. Small business has played a key role in the growth process, and recent trends suggest an expansion of opportunities for small business in smaller rural communities.

In the planning for future growth, public policymakers need to be aware of the very diverse growth pattern that has developed throughout the South. Recent growth trends call into question policies based on a strategy of regional growth centers, in which growth at certain urban nodes is thought of as necessary for regional progress. At the same time, Birch’s research raises doubts as to the effectiveness of regional growth promotion plans aimed solely at major, established corporations—large established firms are responsible for the creation of relatively few jobs. Instead, to accommodate the present pattern of regional growth, present assistance programs need to be restructured to reach small, young firms in outlying areas, beyond the metropolitan border.

Specific guidelines on how to structure assistance programs for small business in nonmetropolitan areas are difficult to formulate. An effective program must be geographically dispersed to deliver a wide range of assistance programs in small communities and rural areas throughout the region. The Department of Agriculture provides a model of a government program designed to deliver capital and technical assistance through its network of county extension agents. If this same network of county extension agents could be
enlisted to help provide assistance to small businesses in rural areas, such a program would have a significant impact on the future growth of southern employment and income.
REFERENCES


This paper will attempt to identify some of the causes of the energy problems faced by small business and the nation today. The dimensions of the problem to the American economy will be presented and the relevance to small business outlined. In order to accomplish these goals a brief overview of the energy problem is provided, followed by a discussion of energy use in the country and Region IV. Finally, the implications to small business are presented. The intent is not to give specific solutions to the problem, but rather to provide the reader with a framework in which to make informed, intelligent decisions. This is an extremely complex issue and I discuss what I believe to be the salient aspects of the problem and admittedly there will be disagreements concerning emphasis.

1. ENERGY OVERVIEW
   
   Industrialization

   The industrial revolution was based upon replacing human power with mechanical power. The revolution began with the harnessing of water and wind power. The emphasis changed to the fossil fuels with the development of the steam and internal combustion engines. Wood as the primary source of steam-generated energy was replaced by coal and then petroleum and natural gas.

   Now the fossil fuels are being challenged by nuclear power, currently fission and eventually by fusion, considered the ultimate energy source by many
physicists. The fossil fuels and nuclear fission represent non-renewable sources of energy. Whereas nuclear fusion, solar, hydro, wind and biomass represent renewable energy sources. Unfortunately, to date these renewable sources have not received the financial support that the non-renewable sources have. Reasons for this lack of attention to renewable energy sources will be given later in this section.

Changing Energy Prices

October 1973 is the generally accepted point where the U.S. moved from facing steadily declining energy prices to ever increasing ones. The immediate factors determining this point are outlined in the discussion of the socio-political aspects of the problem. Here the economic consequences are considered. The changing price of energy has had demonstrable impacts on the U.S. economy, helping to fuel the fires of inflation and to increase the ranks of the unemployed.

Since 1973 industrial energy costs have risen over three times faster than the rate of inflation. Between 1973 and the end of 1978 overall prices increased by 44 percent, whereas industrial energy costs went up by more than 140 percent. Thus energy costs to business have been increasing in both absolute and relative terms. Business has adapted its energy consumption patterns in response to the changing price of energy. According to the most recent data reported in the Annual Survey of Manufacturers: Survey of Fuels and Energy Consumed, between 1971 and 1976 the amount of energy consumed per dollar of value added increased by 64 percent, from 3.3 cents to 5.4 cents, while industrial energy prices increased by 130 percent. Thus business responded to the changing price of energy by adapting its production processes.

The flexibility of business to adapt production to reflect changing energy prices has been the subject of many recent economic studies. The
concern basically is whether or not there exists a fixed relationship between total production and energy consumption. The results thus far have been mixed with some of the analyses supporting the conclusion that the relationship is relatively fixed while others indicate that other factor inputs, such as labor and capital, are substitutes for energy. These latter studies conclude that the historically low price of energy in the U.S. has resulted in domestic industry using roughly twice the amount of energy per dollar of output as required by other industrialized nations. The implications are that the disproportionate use of energy in this country is the result of business and industry responding to the price system rather than being merely a function of the level of industrialization. Economic theory and mounting evidence tends to support the conclusion that substitution among factor inputs will occur naturally as relative factor prices change.

A simple example which has everyday relevance may serve to illustrate this point. The question is how do consumers respond, if at all, to gasoline prices? About 17 percent of the U.S. energy consumption is used for personal transportation, i.e., the private automobile. From the end of World War II up until October 1973 the relative (or real) price of gasoline steadily declined along with all other energy prices. Subsequently, we have experienced continual and recently dramatic increases in the price of gasoline. Has this changing price pattern had any effects? The answer is emphatically, yes. First, people are apparently driving less with gasoline consumption down by between five and ten percent from last year. And second, the sales of the new, more fuel-efficient cars have jumped leaving automobile dealers with growing inventories of the large, "gas-guzzlers." Gasoline demand is an example of a derived demand. It is derived from the need for transportation and is based upon the types of automobiles being used.
The average life of an automobile is roughly 10 years and thus the efficiency of the existing stock of automobiles should reflect this fact, which it does. Since the average vintage of the automobile stock is the year 1969, the miles per gallon (efficiency) represents the MPG of automobiles constructed in that year. Purchasers of new cars in 1969 faced a long period of declining gasoline prices. Thus fuel economy was less important than convenience and comfort to those 1969 automobile buyers. The concurrent downward trends of declining gasoline prices and efficiency of new cars continued until the 1973 oil embargo. As the real price of gasoline has increased since then by over three percent per year and because of the imposition of mandatory mileage standards for all new cars, consumers are switching to the smaller, more efficient vehicles. However, the transition of the entire stock of automobiles will take many years.

The point of the example is that although consumers can be expected to respond rationally to the increase in the real price of gasoline by driving less and switching to more efficient automobiles, the problem will not be resolved quickly. In the broader context also the energy problem represents a long term continuing one. Attempting to ignore it will only serve to make it worse. Continuance of government price controls may provide temporary benefits for certain segments of the economy while serving to exacerbate the long-run problem by forcing the inevitable adjustment of the economy to be postponed. The transition to a more fuel efficient economy will be difficult; all the more difficult the longer it is postponed. Allowing the price system to function freely will serve to facilitate this transition. The rising price of energy will provide the correct signals to business and individuals about the true cost of the resources being used. These price signals will provide the economic incentive to adjust energy consumption patterns to reflect the
realities of the situation. Ignoring the energy issue will not eliminate it as we have discussed thus far.

Socio-political Issues

The timing of the energy crisis, although not necessarily the underlying causes, relate to the situation in the Middle East. The available evidence suggests that the conditions that precipitated the 1973 Arab oil embargo and subsequently led to the increasing strength of the Organization of Petroleum Exporting Countries (OPEC) are still essentially unresolved. The major countries within OPEC in terms of proved petroleum reserves are the Arab nations of Saudi Arabia, Iraq, Kuwait, Abu Dhabi, Qatar, Libya and Algeria. These are the nations which imposed the 1973 oil embargo and which have structured the OPEC cartel's policies according to their perceived social, political and economic goals. The immediate cause of the 1973 embargo was the political situation in the Middle East concerning the disposition of the Palestinian refugees. Those refugees, who were forced to flee their homeland with the establishment of the State of Israel, have been (and continue to be) a destabilizing factor in Arab and non-Arab nations of that area of the world. The political situation in the Middle East remains highly volatile after more than thirty years. The nations surrounding Israel have borne the burden of the Palestinian resettlement while Israel has been subjected to sporadic commando strikes and three devastating wars. Middle East politics have thus become a critical factor in an energy dependent world.

These political factors have been reinforced by social and economic considerations. The petroleum-rich countries of that area watched much of their wealth being exported to the rest of the world with only small payments made in return. Their recognition of the industrialized nations dependence upon petroleum-derived energy provided OPEC with the means to increase oil
prices and oil revenues. In 1973, OPEC first exercised this latent power by raising the price of crude oil from $3.00 to $5.11 per 42 U.S. gallon barrel. Again in January 1974, OPEC increased the price of oil to $11.65 per barrel. Regular price increases have been imposed since then until now, August 1979, where the spot price of oil has exceeded $40.00 per barrel.

There is every reason to believe that these price increases will continue and little reason to suspect the continued viability of the cartel since it has proved itself now over a period of six years. OPEC can continue being an important factor influencing the industrialized countries because we have done so little to date to make fundamental changes in our economies. The recent turmoil in Iran has served to further strengthen the OPEC position and illustrate the continued failure of the West to adapt to the new realities concerning energy. Essentially we find nationalistic and economic factors in the Middle East supporting and reinforcing institutional and economic factors in the industrialized nations.

Institutional Factors

One result of division of labor and industrialization has been the creation of large companies. Large domestic companies seeking new markets for their products have lead to the evolution of multi-national companies. These multi-nationals have been founded to secure a profit for their investors and this has lead to the divergence between corporate and national goals. This can be seen clearly in the energy field. The actions of the multi-national oil firms have supported the edicts of the OPEC cartel with respect to prices and supply. A review of the profits of the oil companies indicates that the higher OPEC prices are quickly converted to higher corporate profits. The conclusion that the major oil companies have a vested interest in the continued viability of the OPEC cartel is inescapable. In addition, these multi-national
companies cooperated with and were, in fact, the sole mechanism for enforcing the 1973 oil embargo. The OPEC nations had no means for insuring the integrity of the embargo since they did not control the distribution of crude oil. The multi-national companies, then and now, controlled the distribution network. Therefore the companies alone could monitor the embargo. The industrialized nations also relied upon oil company data to assess the impact of the embargo. This reliance upon petroleum industry statistics continues today.

But more important than controlling the data regarding oil, the industry production is highly concentrated in only a few firms. As the late John W. Blair cites in The Control of Oil, in 1970 the eight largest petroleum companies accounted for 64 percent of U.S. reserves, 50 percent of U.S. production, 58 percent of U.S. refining capacity and 55 percent of U.S. retail sales. Such concentration ratios are one means of evaluating the structure of an industry. The higher the ratio the more concentrated is the industry's activity within a few firms. These statistics reported by Blair indicate that the petroleum industry is a highly concentrated one in all stages of operations from well-head through refinery to the final consumer. The term applied to a highly concentrated industry is oligopoly. Oligopolies by nature are able to exert market power thereby reducing production levels and increasing prices from what would exist in a competitively structured industry. The oil companies vigorously deny either that they are oligopolies or that they exert any influence on the market. It seems however undeniable that the majors dominate the industry and that their impact has been to reduce the amount of competition.

The success of the Texas Railroad Commission (TRC) is perhaps the best example of the attitude of the companies toward competition. The TRC was established with the sole purpose to stabilize prices for crude oil. The way
this is done is to regulate the amount of oil which can be pumped from the ground. The major oil companies actively support the TRC since the destabilizing impact of wide and frequent variations in price are quickly reflected in major profit fluctuations. As it has operated, the TRC is really the administrative mechanism of the major oil companies for controlling prices and profits.

The final institutional point to be considered has to do with the energy industry in general. The energy industry is characterized by large companies. The major petroleum firms own coal and uranium mines. Electric utilities are large companies too. This industry structure with a few large companies effectively works against technologies which do not require gigantic scales of plant. Many renewable energy sources such as solar technologies will only be efficient at small scale. For example, solar water heating is now economic for individual houses or buildings. However, the government and industry are sponsoring multi-million dollar solar projects designed to replicate existing centralized power facilities. The effective use of solar energy would seem to dictate decentralization with emphasis on units scaled to serve individual buildings, not whole cities. However, the dominance of the energy field by large companies has resulted in the most research money being concentrated on large scale projects consonant with the existing structure of the industry. We are discovering that higher levels of technology do not necessarily require larger and larger scale of plants. The growing power of microprocessors is effectively challenging this heretofore accepted relationship. It is becoming economical for small business to computerize without having a large central computer. The same is true in many of the renewable energy alternatives. Small in reality is becoming beautiful.
Summary of Energy Problem

In summary, the factors leading to the existing energy problems which we face today are a result of the interaction of four major factors. First, the industrial revolution created the demand for energy. This, combined with the declining price of energy, led to the reliance on energy-using equipment and processes. The relatively cheap energy consumed in the U.S. has resulted in the creation of the existing stock of energy inefficient capital equipment. Replacing this stock of equipment will take a long time. Third, the rising tide of nationalism in the world and the politics in the Middle East have allowed oil producing countries to benefit from the industrialized world's dependence on energy. Continued strength of the OPEC cartel and future energy price increases are to be expected. Finally, the dominance of the energy industry by large companies has to date mitigated against small-scale alternative energy sources being developed. Hopefully this will change in the future.

The next section of this paper will examine industrial use of energy in the nation and specifically within Region IV.

2. ENERGY USE PATTERNS

Describing in any detail national or regional energy consumption patterns is extremely difficult because of the paucity of reliable data. The federal government only started collecting fuel specific data through the Annual Survey of Manufacturers in 1972. Most previous energy data were those developed by industry trade associations and there was little attempt at achieving consistency either with respect to definitions or time period covered. Thus problems arise when attempting to develop aggregate end-use information. Data developed by the Bureau of Mines and Resources for the Future show that in 1975 roughly 39 percent of energy use is in the manufacturing sectors of the
economy. The balance of the 62 percent of the energy used for production is
distributed between commercial and freight activities. And of the 38 percent
devoted to personal consumption, 21 percent was used in the home and 17 percent
in passenger transportation. Since the most complete energy data are available
for manufacturing enterprises and because manufacturing represents the largest
aggregate energy-consuming sector, the following discussion will focus on it.
The presentation will be in terms of general industry groupings using the
Standard Industrial Classification (SIC) codes to define industries. It is
necessary to look at these broad aggregates rather than more specific
definitions, again because of the data problems.

Such aggregation means that the statistics discussed are industry
averages with some firms within each industry necessarily performing better
than and some firms performing less well than this average figure. Many
factors contribute to a particular firm's performance such as location, age
of plant and facilities, and managerial abilities. All these differ among
firms within an industry. Unfortunately, the data are not currently available
to analyze these differences. A final element affecting the analysis is
that many factors are changing over time. While we are concerned with the
impact of changing energy prices and energy availability, comparison of pre-
and post-energy crisis data includes changes in these other factors as well.
Technology and consumer tastes are but two examples of factors which continue
to change dramatically. All of these changes affect both usage patterns
of inputs into the production process and potentially each other factor as
well, e.g., technology affects consumer tastes and vice versa. Therefore,
out of necessity, this discussion will focus only upon the effects of
changing energy prices on the production process, abstracting from the other
changes which have occurred.
Response to Price Changes

Since we are dealing with a market oriented economy, information about how supply and demand relationships react to the changing energy situation is of primary interest. The supply of a good offered for sale is determined from the cost of producing the item. These production costs are themselves determined by: 1) the prices of raw material inputs; 2) the age of the production facility; 3) the level of technology in the industry; 4) the skill of management; and 5) the flexibility to change production procedures among other factors. On the demand side of the market equation, consumers purchases are affected by: 1) the product's price; 2) the prices of other goods; 3) income levels; and 4) consumer tastes. Fortunately, the concepts of supply and demand can be quantified and specified as mathematical functions. This greatly facilitates analyzing the effects of price changes on the quantities supplied or demanded.

Such analysis is couched in terms of elasticity of supply or demand. Elasticity is a dimensionless measure of the responsiveness of producers and consumers to changes in any of the quantity determining variables mentioned above. The definition of elasticity is the ratio of the percentage change in quantity supplied (or demanded) to the percentage change in one of those variables, i.e., price, income, tastes, etc. For example, the own-price elasticity of demand for natural gas measures how consumers respond to changes in the price of natural gas. As the price increases, consumers wish to consume smaller and smaller amounts of natural gas. Table 1 presents the own- and cross-price elasticities of demand for various fuels used in the residential-commercial and industrial sectors. The information in Table 1 indicates that if the residential-commercial consumer faces a price increase in natural gas of 1 percent, consumption of natural gas in the short-run (SR - 1 year) will
TABLE 1
U.S. PRICE ELASTICITIES FOR ENERGY

<table>
<thead>
<tr>
<th>CONSUMPTION</th>
<th>PRICE</th>
<th>NATURAL GAS</th>
<th>OIL</th>
<th>ELECTRICITY</th>
<th>COAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Residential-</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Natural Gas</td>
<td>SR</td>
<td>-0.15</td>
<td>0.01</td>
<td>0.01</td>
<td>--</td>
</tr>
<tr>
<td></td>
<td>LR</td>
<td>-1.01</td>
<td>0.05</td>
<td>0.17</td>
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</tr>
<tr>
<td>Oil</td>
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<td>-0.18</td>
<td>0.01</td>
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</tr>
<tr>
<td></td>
<td>LR</td>
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<td>-1.12</td>
<td>0.16</td>
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</tr>
<tr>
<td>Electricity</td>
<td>SR</td>
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<td>0.01</td>
<td>-0.19</td>
<td>--</td>
</tr>
<tr>
<td></td>
<td>LR</td>
<td>0.17</td>
<td>0.05</td>
<td>-1.00</td>
<td>--</td>
</tr>
<tr>
<td>Industrial</td>
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<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Natural Gas</td>
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<tr>
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<td>-0.11</td>
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</tr>
<tr>
<td></td>
<td>LR</td>
<td>0.75</td>
<td>-1.32</td>
<td>0.34</td>
<td>0.14</td>
</tr>
<tr>
<td>Electricity</td>
<td>SR</td>
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<td>0.01</td>
<td>-0.11</td>
<td>0.01</td>
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<tr>
<td>Coal</td>
<td>SR</td>
<td>0.06</td>
<td>0.01</td>
<td>0.03</td>
<td>-0.10</td>
</tr>
<tr>
<td></td>
<td>LR</td>
<td>0.75</td>
<td>0.14</td>
<td>0.33</td>
<td>-1.14</td>
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</tbody>
</table>

SOURCE:

decline by 0.15 percent and in the long-run by 1.01 percent. Thus these consumers show only a small response to short-run changes in price but a somewhat larger response in the long-run.

What reasons cause this type of consumer behavior? Well, one important reason is that it takes time to convert from burning one kind of fuel to
another. Essentially, it is the same stock problem that exists with respect to automobiles. There is an existing stock of energy-using equipment which can operate well only within defined limits. Second, time is required to make new contracts with alternative fuel suppliers. And third, there may be technical constraints, either legal or purely physical ones, which serve to delay conversion. Finally, a short-run price change may be viewed as only a temporary phenomena which could be reversed in the future. All these considerations contribute to the general conclusion that in the short-run response to energy price changes will be less than in the long-run. To put it more technically, the own-price elasticity of demand is more inelastic in the short-run than in the long-run.

Inelastic demand simply means that the percentage change in quantity is less than the percentage change in price. Conversely, if the percentage change in quantity exceeds the percentage change in price, demand is said to be elastic (or responsive to price changes). You should notice that all the short-run own-price elasticities of demand shown in Table 1 are inelastic, i.e., falling in the range from 0 to -1. Four of the long-run own-price elasticities of demand are elastic being less than -1, while three are inelastic.

The three exceptions are industrial natural gas use, residential-commercial natural gas and electricity. The industrial natural gas anomaly probably exists because some manufacturing processes are not readily available. The same reasoning would apply to the residential-commercial electricity case. There exists no substitute energy source for electricity in many cases, e.g., how do you operate a television set or lighting without electricity? The residential-commercial natural gas elasticity is close to one most probably because of the cleanliness of that fuel. Natural gas is the cleanest burning of all the fossil fuels and small boilers are much less efficient than larger
ones in assuring total combustion of the fuel. Therefore, where each consuming unit, either private residence or commercial establishment, has its own boilers, it is important to attempt to use the cleanest burning fuel available, i.e., natural gas.

The remaining values in the table, which are all positive numbers, represent cross-price elasticities of demand. They measure the impact on the consumption of one fuel when the price of an alternative fuel changes. Thus an increase in the price of oil by one percent will, in the short-run, result in industry reducing its consumption of oil by 0.11 percent (the own-price effect) and increasing its consumption of other fuels by about 0.01 percent (the cross-price effects). In the long-run the price induced impacts would be greater, namely 1.32 percent reduction in oil use by industry and between 0.13 and 0.14 percent increases in the use of natural gas, electricity and coal. Thus elasticity values merely summarize the effects of changing the relative prices of fuels on usage patterns. As the price of oil increases relative to the price of other fuels in the long-run industry will attempt to substitute the relatively less expensive fuel. In addition, it can be seen that firms are working to conserve energy consumption in general because the reduction in oil consumption is not being totally offset by increases in consumption of the other fuels.

A final insight is provided by the Table 1 elasticities is that generally, in the short-run, residential-commercial consumers of energy generally show more responsiveness to price changes than does industry. In the long-run, the opposite is true. The implication is that higher energy prices will elicit a response from individuals first as they attempt to adjust their spending patterns. However, in the long-run industry will be better able to adapt to the changing price of energy. The inference that
may be drawn is that consumers are able to instigate quickly some conservation measures, while in the long-run they are not really able to make fundamental changes in the way they use energy. The opposite is true for business. Simple conservation is more difficult if output is to be maintained in the short-run. Business does have, however, a greater ability in the long-run to develop and use more energy-efficient machinery than do individuals.

In general, the same stock phenomena operates with respect to gasoline demand. Namely, in the short-run there exists a stock of automobiles which have particular efficiency characteristics. The short-run response of drivers to gasoline price increases will be to drive these existing vehicles less. In the long-run, however, if the price change is viewed as permanent, consumers will retire the energy-inefficient vehicles and replace them with more efficient ones. In addition, alternative transportation systems will be developed, e.g., mass transit, and new commuting patterns will evolve. These will all contribute to a more elastic long-run demand for gasoline.

Consumption Changes

Industrial energy consumption has changed as energy prices have changed. Much of the energy debate is couched in terms of quadrillion British Thermal Units (BTU's) or quads. A quadrillion is the number 10 with fifteen zeros following it. The concept of quads was developed to allow adding up the energy use when this energy was derived from different fuel sources. Serious questions exist concerning the appropriate weights to apply to different fuels to allow this aggregation, but we will not address these. Rather we will accept the aggregation procedure in order to be able to focus on the broader problem.

In 1971, industrial consumption of energy amounted to 13.1 quads. This declined to 12.6 quads in 1976. This reduction in energy consumption by
industry was accomplished while the value of industrial output was increasing. About $21.12 of value-added was created nationally for every million BTU's consumed by industry in 1971. This increased to roughly $24.25 in 1976. Thus each million BTU's used by industry in 1976 generated slightly over $3.00 more value-added than was done in 1971. And these figures are net of inflation being stated in 1967 constant dollar terms. Industrial energy expenditures increased from $9.2 billion to $16.7 billion over the same interval. This means that, while energy outlays increased at an average annual rate of 9.9 percent, energy consumed per dollar value-added produced declined by about 2.4 percent annually. The increased efficiency in overall industrial use of energy in Region IV has not been as dramatic as the national experience. Much of this difference may be attributed to the differing industry mix between Region IV and the nation as a whole.

Whereas Region IV produces fewer dollars of value-added per million BTU's than the national average for manufacturing, in some sectors it is consistently more efficient. Food and kindred products is an example in which Region IV apparently enjoys a comparative advantage. In 1976, Region IV produced $37.01 of value added per million BTU's in food processing. This was almost 20 percent better than the national average. Region IV's comparative advantage in 1971 was only 16 percent. Fabricated metals is another such example. The Region IV comparative advantage in fabricated metals increased from 8 percent better in 1971 to 14 percent more efficient energy use in 1976. The opposite has occurred in other sectors such as petroleum and rubber. In these sectors, Region IV has lost ground vis a vis the rest of the nation. Unfortunately, no clear trends are yet evident. Table 2 shows national and Region IV BTU consumed ratio, value-added, for the year of 1971-1976.
TABLE 2
VALUE-ADDED/ENERGY RATIO IN MANUFACTURING
(dollars per million BTU's)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>20</td>
<td>Food &amp; Kindred</td>
<td>$28.85</td>
<td>$33.50</td>
<td>$30.96</td>
<td>$37.01</td>
</tr>
<tr>
<td>21</td>
<td>Tobacco</td>
<td>120.39</td>
<td>135.40</td>
<td>124.71</td>
<td>142.98</td>
</tr>
<tr>
<td>22</td>
<td>Textile Mills</td>
<td>24.32</td>
<td>23.95</td>
<td>26.46</td>
<td>25.30</td>
</tr>
<tr>
<td>23</td>
<td>Apparel</td>
<td>164.52</td>
<td>120.67</td>
<td>179.04</td>
<td>142.65</td>
</tr>
<tr>
<td>24</td>
<td>Lumber &amp; Wood</td>
<td>25.61</td>
<td>17.38</td>
<td>32.74</td>
<td>23.27</td>
</tr>
<tr>
<td>25</td>
<td>Furniture</td>
<td>76.14</td>
<td>94.14</td>
<td>92.97</td>
<td>101.45</td>
</tr>
<tr>
<td>26</td>
<td>Paper and Allied</td>
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<td>5.78</td>
<td>9.58</td>
<td>7.36</td>
</tr>
<tr>
<td>27</td>
<td>Printing &amp; Publishing</td>
<td>155.71</td>
<td>120.62</td>
<td>189.83</td>
<td>172.20</td>
</tr>
<tr>
<td>28</td>
<td>Chemicals</td>
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<td>8.85</td>
<td>10.39</td>
<td>8.76</td>
</tr>
<tr>
<td>29</td>
<td>Petroleum</td>
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<td>6.71</td>
<td>6.02</td>
<td>6.76</td>
</tr>
<tr>
<td>30</td>
<td>Rubber</td>
<td>37.22</td>
<td>41.63</td>
<td>41.06</td>
<td>41.97</td>
</tr>
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<td>31</td>
<td>Leather</td>
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</tr>
<tr>
<td>32</td>
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<td>7.08</td>
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<td>7.65</td>
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<td>33</td>
<td>Primary Metals</td>
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<td>7.09</td>
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</tr>
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<td>34</td>
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<td>59.77</td>
<td>62.26</td>
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</tr>
<tr>
<td>35</td>
<td>Machinery</td>
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<td>Elec. Equipment</td>
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<td>80.25</td>
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</tr>
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<td>37</td>
<td>Trans. Equipment</td>
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</tr>
<tr>
<td>39</td>
<td>Miscellaneous</td>
<td>80.35</td>
<td>68.26</td>
<td>116.13</td>
<td>115.94</td>
</tr>
</tbody>
</table>

Manufacturing Average $21.12 $20.37 $24.25 $21.68

However, it is true that on average relatively more energy is used per dollar of value-added produced in Region IV than in the nation. Rather surprisingly, this difference increased between 1971 and 1976 from about 4 percent greater to about 12 percent greater. Interpreting this is rather difficult. The conventional wisdom holds that areas of the country enjoying warmer climates and having indigenous supplies of energy will suffer the least and perhaps benefit the most from the energy crisis. Whether this is true or not cannot be demonstrated by the available data. Unquestionably there has
been a shift of economic activity from the Northeast and Midwest to the "Sun-Belt." Whether, and how much, this shift has been accelerated by the energy crisis, is open to debate. And the specific effect on Region IV is also unresolved. Before the issue of climate is addressed, let us look at energy consumption by manufacturing sector.

Tables 3 and 4 present data for the individual states in Region IV and the nation for the years 1971 and 1976, respectively. Over this time interval, consumption of energy by U. S. manufacturers declined from 13.1 quads to 12.6 quads. The Region IV consumption increased slightly from 1.9 quads to 2.0 quads. Because there is incomplete reporting of information at the state level for major industry groups due to disclosure problems, all that can be said is that there was no appreciable change in industrial energy consumption within Region IV. Region IV did, however, increase its proportion of total national consumption from 14.8 percent to 16.1 percent.

Major concern focuses upon the most energy-intensive industry sectors: 1) food and kindred products; 2) paper and allied products; 3) chemicals and allied products; 4) petroleum and coal products; 5) stone, clay and glass products; and 6) primary metal industries. These six industries represented over 80 percent of total industrial energy consumption in 1976, i.e., about 10.2 quads, and this figure is relatively unchanged from 1971. Modern industrial society is founded on these sectors: petroleum, chemicals, and primary metals; and a convenience-oriented consumer society relies on glass and paper products for packaging and on food processing. Small businesses represent significant elements of the food, the paper, and the stone, clay and glass industries. Overall, small business accounts for about 13 percent of all sales in the manufacturing sectors. In retail trade, of which small business (less than 100 employees) represents about 59 percent of sales, it
### TABLE 3

**PURCHASED FUELS AND ELECTRICITY, 1971**

*(trillions of BTU's)*

<table>
<thead>
<tr>
<th>Manuf. Sectors</th>
<th>AL</th>
<th>FL</th>
<th>GA</th>
<th>KY</th>
<th>MS</th>
<th>NC</th>
<th>SC</th>
<th>TN</th>
<th>Region</th>
<th>U.S.</th>
<th>%</th>
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</thead>
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<td>27.6</td>
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<td>6.8</td>
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<td>17.1</td>
<td>110.2</td>
<td>1025.6</td>
<td>10.7</td>
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<tr>
<td>Tobacco</td>
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<td>--</td>
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<td>--</td>
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<td>1.4</td>
<td>1.4</td>
<td>3.4</td>
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<td>20.5</td>
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<td>--</td>
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<td>2.0</td>
<td>11.5</td>
<td>60.7</td>
<td>18.9</td>
</tr>
<tr>
<td>Paper &amp; Allied</td>
<td>73.0</td>
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<td>8.2</td>
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<td>317.7</td>
<td>1937.1</td>
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2/ Billions of KWH equivalent converted by multiplying by 3.412

3/ Estimates

4/ Columns will not sum to totals because of mission data.
### TABLE 4

**PURCHASED FUELS AND ELECTRICITY, 1976**

(trillions of BTU's)

<table>
<thead>
<tr>
<th>Manuf. Sectors</th>
<th>AL</th>
<th>FL</th>
<th>GA</th>
<th>KY</th>
<th>MS</th>
<th>NC</th>
<th>SC</th>
<th>TN</th>
<th>IV</th>
<th>Totals</th>
<th>U.S.</th>
<th>%</th>
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2/ Estimates

3/ Columns may not sum to totals due to rounding.
is estimated that 1.2 quads of energy were consumed in 1974, with finance, insurance, and real estate consuming another 1.1 quads. Small business is directly concerned with almost 80 percent of energy consumption. As U. S. Senate and House of Representatives hearings have indicated, small business is concerned about the price and availability of energy.

Within Region IV, these same energy-intensive industries accounted for 75 percent of the manufacturing energy use or about 1.5 quads. The chemical industry alone accounted for over one third of that amount. A significant proportion of the chemical industry is made up of small business. And it can be seen from Table 2, that relative (and absolute) competitiveness with the rest of the nation has declined between 1971 and 1976. While the energy efficiency of chemical production improved by 11 percent in the nation as a whole, efficiency in Region IV actually declined slightly. This can also be seen from the data in Tables 3 and 4: the national percentage of energy used in the chemical industry by Region IV firms increased from 17.9 percent to 18.7 percent.

Effects of Climate

We know that climate affects industrial energy consumption and some analysts have suggested that the energy crisis would reinforce migration to the Sun-belt. If this is the case, will Region IV be expected to benefit? Table 5 provides some climatic data for Region IV and the U.S. It can be seen that while the region has milder winters, it also has more severe summers. The annual average daily temperature for our area of the country is 10 degrees warmer than for the nation. However, in terms of heating and cooling degree days a slightly different picture is seen. Average daily temperatures below 65 degrees Fahrenheit are classified as heating degree-days, while those above 65 degrees are termed cooling degree days. Region IV enjoys only 53
## Table 5
CLIMATIC COMPARISONS BETWEEN REGION IV AND THE U.S. AVERAGE

<table>
<thead>
<tr>
<th>Month</th>
<th>Average Daily Temperature (degrees Fahrenheit)</th>
<th>Heating Degree Days</th>
<th>Cooling Degree Days</th>
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<td>U.S.</td>
<td>Region IV</td>
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<td>113</td>
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<tr>
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<td>Annual Average</td>
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</table>


2/ Areal weighted

3/ Population weighted
percent of the national average heating degree days, however, it suffers 87 percent more cooling degree days. Will the warmer winters attract more economic activity than the hotter summers repel? Obviously, it is misleading to categorize the eight states within the region as having similar climates. Florida and Mississippi have more cooling degree days, 3358 and 2236, respectively, and fewer heating degree days, 689 and 2375, respectively, than the regional average. The climate of the region alone will probably not serve to attract major new industry. Only Florida can be expected to benefit from increased migration of retired people. However, the rest of the region cannot expect to benefit mainly because of the need for air conditioning. Thus summer fuel costs in large portions of this area exceed winter heating bills. This factor should serve to mitigate against firms moving to the area merely because of fuel costs.

The other factors such as lower regional labor costs and site costs for new plants will continue to serve as a growth stimulus to the area. Particularly, now that industry is faced with replacing older, less energy-efficient machinery. The Midwest and Northeast generally have the older manufacturing facilities which need replacement. Rising energy costs will reinforce the effects of regional wage and land value differentials, thus increasing the shift of economic activity away from these other areas. The fastest growing regions in the 1980's are expected to continue to be in the Sun-belt and the West. Some of this anticipated growth will undoubtedly accrue to Region IV. Whether the energy crisis will have any substantial impact on this region is questionable. Since 1973, the region has been growing at roughly the national average. Further oil price increases may change this although most probably not to any great extent.
Supplies of Energy

Within Region IV only Kentucky has any substantial energy reserves—coal. Unfortunately, much of Kentucky coal is high in sulfur content and therefore, its expanded use will pose severe environmental problems. These problems with coal led to the shift in the early 1960's to the cleaner burning fuels, oil and natural gas. The President and the Department of Energy (DOE) foresee an increasing dependence on coal. Mr. Carter has even suggested that some environmental regulations may be in need of change. The alternative uses of coal being favored by the Administration involve creating synthetic substitutes for oil and natural gas through various processes of liquification and gasification. These processes themselves involve environmental costs, so they may require a long time to develop.

A coal-oil-water mixture is under development now which may address some of these problems. It has been found that powered coal will remain suspended in an oil-water mixture if the mixture is subjected to ultrasonic vibrations. The solution appears to remain stable indefinitely. And it is argued that because the coal is finely ground, more complete burning occurs, thereby potentially eliminating the need for stack scrubbers. This process, developed at the University of Louisville, still needs to be field tested. If these tests are successful, we will be able to extend substantially our supplies of oil.

The Tennessee Valley Authority represents the only other major energy source in Region IV. This is hydroelectric power. The potential for additional hydro facilities is limited. It is interesting to note that much of the electric energy consumed in Kentucky and Tennessee is diverted to the nuclear industry for the uranium processing and enrichment required both for weapons use and electric power stations. Roughly half of the electricity generated in
the State of Kentucky is destined for the Paducah facility of DOE. This fact results in Kentucky being a net importer of electricity. It appears that indigenous energy supplies will probably not serve to attract new activities to the region.

3. FUTURE ENERGY NEEDS

Forecasts

The forecasts of energy demands published by the Federal Government and those prepared by private groups are generally rather optimistic about the ability of the economy to adapt successfully to the new energy situation. The DOE forecasts indicate that energy consumption will grow at an annual rate of 2.1 percent to the year 1980. Similar, Chase Manhattan Bank forecasts energy consumption in the year 2000 of 138 quads, a growth rate of 2.6 percent annually. Both forecasts are optimistic because they indicate a reduction in rate of growth of energy consumption and a switching from reliance on petroleum and natural gas to nuclear and coal. Preliminary data tends to support their conclusion regarding an increased efficiency in the use of energy, but the switching question is yet to be resolved, particularly in light of the recent Three Mile Island accident and historical opposition to coal.

The DOE forecast reports growth rates by fuel type and end-use sector. The data published in the Energy Information Administration 1977 Annual Report to Congress shows industrial and raw materials energy use growing at 3.5 and 6.3 percent annually, respectively, through 1990. Residential and transportation use grows at only 1.7 percent and 1.5 percent annually. And commercial energy consumption is forecast to grow at the annual rate of only 0.7 percent.

More pessimistic forecasts that led to "doomsday" predictions have been prepared by Meadows, Forrester and the Club of Rome. These modern day
Malthusian's rely upon the relatively simplistic assumption that past trends will inexorably continue into the future. As we have seen, the evidence is to the contrary. Substitution has occurred since the scarcity of energy has been recognized and energy has become more expensive. Individuals and business adjust their behavior with the resultant dramatic decline in the rates of growth in energy consumption. During the 1960's six to nine percent annual increase in electricity consumption was the norm. The DOE forecasts anticipate electricity demand to increase by less than 4 percent annually over the next decade. It is easy to comprehend the divergent results obtained if the forecasting methodology is known. The naive forecasts based on simple trend extrapolation do not allow for changes in human behavior. The economy has and will continue to adapt. The econometric techniques used by DOE and Chase recognize and rely upon this ability.

**Transition**

Initially, the adaptation will take the form of pure conservation. Existing machines will be used less and more efficiently. Carpooling and other forms of mass transit will see increased usage. Lighting will be turned down and off when not needed. Reducing the illumination in many work areas and retail stores can substantially decrease electricity consumption without adversely affecting productivity or safety. Warmer settings for thermostats in summer and cooler settings in winter will save additional fuel. The Presidentially mandated 78 degrees in the summer and 68 degrees in the winter recognizes this fact. More direct forms of energy management are becoming economically available to the small business with the availability of inexpensive microprocessors. Small business enterprises use these devices now for word processing, mailing lists, payrolls and taxes, and inventory control. These small computers can also monitor and control energy use. Most new
automobiles incorporate one or more of the microprocessors to monitor gasoline flow and to reduce engine emissions. Microprocessor technology promises the advantages of energy management at affordable prices for small business.

In the longer run, buildings and equipment will be redesigned for more efficient energy use. As older equipment is replaced, attention will focus more on the energy requirements of the new machinery than was the case in the past. New buildings will be better insulated and most probably will include both passive and active solar energy devices. Here we will see a major change from the current large-scale energy facilities to units designed to serve the needs of individual businesses. Small plants and stores will be able to provide for a portion of their energy needs through solar devices. Co-generation of power will be expanded. The heat which is now wasted in the process of generating electricity will be used for space heating. Plants that use boilers for processing will use some of the now wasted heat for other purposes.

A reversal of the trend toward increasing urban sprawl should be expected over the next two decades. Revitalization of our decaying central cities would substantially reduce the country's energy needs and allow more widespread use of co-generation of power. These implications are significant to many small businesses, because the current wide dispersal of retail outlets probably cannot be sustained. A particularly hard hit sector may be the drive-in restaurant and those activities catering to automobile travellers. The interstate highway system changed American life and living patterns, but this change was founded on cheap energy. With energy becoming relatively more expensive, the trends fostered by modern highways will not continue.

The adjustments that individuals make in their daily living patterns will shape the small business activity of the future. In Region IV, the
movement will be away from increasingly dispersed suburbs toward higher
density living patterns. And small business must be ready and prepared to
adapt to these inevitable changes.

Summary

The outlook is relatively good since the American economy has always
demonstrated considerable ability to adjust. The future adjustments still
needed will not be costless however. Individual expectations must be changed
to reflect the new energy realities and this necessarily means that life
styles will change. Region IV may be in a relatively better position to
adapt to these new energy realities than other areas of the country because
it is not as locked-in to the past. This flexibility should serve as a
positive stimulus to the area as a whole.

The industrial revolution and cheap energy has encouraged Americans to
use energy wastefully. The socio-political realities in the world today will
result in ever higher energy prices. Therefore we must adjust our living
patterns and our production processes to reflect these changes in energy
availability and price. The adaptation will take time to implement and will
be expensive. Failure to accept the realities of the energy crisis cannot
be allowed to occur. Small business can lead the way by effectively
demonstrating its willingness to adjust. One of the strengths of the free
enterprise system is its inherent ability to change. The energy crisis may
well prove its greatest challenge.
Selected References

Books and Articles


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ORGANIZATION PLANNING AND MANAGEMENT SUCCESION: 
CASES IN SMALL BUSINESS SURVIVAL

Curtis E. Tate, Jr. 
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1. INTRODUCTION

This paper is intended to show the importance of organization planning and management succession. Section 2 discusses the purposes of organization planning while Section 3 covers the question of providing for management succession. Both are illustrated with cases derived from the author's experiences with small business in the Southeast through consulting, counseling, training programs, field case research, and direct involvement with individual business firms' owners/managers.

2. ORGANIZATION PLANNING

Purposes

The importance of sound organization planning can be seen in a review of its several purposes:

To provide for division of labor. In many instances, the small/independent business firm has its beginning as a "one-person show" where the owner/manager is both responsible for "the managing" and "the doing" with no clearly delineated division of activities. As the firm grows in production and personnel, the earlier pattern of behavior tends to continue. It is not uncommon to observe that because of "the doing," management activities are neglected, ignored, or avoided. Each person in the firm seems to do whatever the moment demands with no evidence of thought being given to a partitioning of the activities, i.e., the assignment of a
specific group of work activities to designated individuals. This lack of a clearly defined division of labor serves as a limiting factor in the growth of a firm. In those firms where growth seems to have occurred from the beginning without interruption, little initial consideration appears to have been given the division of labor. Effective division of labor is a basic premise in organization planning.

To Permit Specialization. One finds that not all firms proceed as indicated above. While some firms lack a clearly defined division of labor and the benefits that accrue from the specialization of labor, other firms seem to be organized around the essential skills/expertise required for the firm's existence. In some instances, one finds that a firm owes its inception to one or more specialized skills. Examples of firms whose existence is dependent on specialization are:

a. Small machine shops built around the skills of a machinist, a welder, etc.
b. Sheet metal shops built around a sheet metal specialist.
c. Auction companies built around an auctioneer, clerical, and public relations personnel.
d. Auto repair shop dependent on the skilled auto mechanic.
e. Appliance and T.V. repair shops dependent on the skilled technician.
f. Computer software service firms dependent on the skills of the computer analyst.

Initially, in this discussion, the focus has been on the skilled trades person. In some businesses, because of their diverse nature, a variety of skills may be involved. Whether special or general skills
are needed, the advantage of specialization is the promotion of increased
operating effectiveness with better use of people, time, and other resources.

Management is also an area of specialization that requires identification
and practice. It should be understood that the degree of recognition
 accorded specialization is directly related to the nature of the organization's
 structure.

To provide for direction and control. In those firms observed to
have direction and control difficulties, it seems universal that there is a
lack of organizational planning. Among many business owners/managers there
appears to be an inherent fear of the constraints or rigidity imposed by a
formally developed organizational structure. It has been observed, however,
that with the presence of carefully developed organizational plans, roles
are more clearly understood, and direction and control are better maintained.

To make possible an organizational structure compatible with the
business' mission. Unless the organizational structure corresponds to the
business' mission, the firm's resources are ineffectively utilized. The
quality and ability of personnel relate to the organizational structure. A
definition of roles and activities should be clearly established through
such a plan. This should illustrate that the formal organizational structure
is something besides titles, boxes, and lines on a chart. The organization
is the mechanism that moves the entity's resources toward its objective.
Therefore, the organizational structure must be compatible with the business' mission.

To provide an awareness of the organizational needs of the business.
One should start with the premise that the organizational structure is a
composite of the firm and its activities. Formulation of such a composite
requires an awareness of the firm in totality and the needs essential to
this totality. It is not uncommon to observe a business owner/manager whose
daily activities are so routinized that little thought is given to anything beyond the "doing." A common response, among this group, is that, "planning and organizational activities are unneeded burdens to be left to the more affluent larger firm."

In analyzing the activities of many small/independent businesses, one becomes aware of the confusion, conflicts, frustrations, and disarray in the activities. In many instances the cause of this environmental state is so apparent the question comes forth, "Why doesn't the owner/manager see how to resolve the difficulty?" The solution is carefully structured organizational planning and implementation. Surely, there exists a need to compliment the organizational planning with positive training to enable each member of the organization to understand their assigned tasks and how those tasks must be carried out. Example: How many times have you observed this dilemma among the waitresses and cooks in a restaurant? In contrast, to that dilemma is the flow of activities where obvious order due to the organizational structure and planning created a pleasant environment for customers and employees alike.

To define roles. Formal organizational structure exists when thoughtful, detailed analysis of the organization's mission is followed by planning and developing the organization's structure accordingly. It is this process that enables one to identify the roles and to define their dimensions. When this approach is used the problems of communication, as applied to the individual in their roles are simplified; the understanding of responsibility and authority is clarified; the functioning of the firm is more effective; and the objectives are more readily achieved, based on collective performance of the individuals in their roles.

To define relationships. It has been frequently observed, that the lack of a well-defined formal organizational structure causes confusion and
conflict between individual employees concerning the status of their relationships. The ill-defined relationships raise questions concerning authority and roles of individual employees as in the case where two people were each given the impression that they headed the same area of activity to which they were assigned. The firm's head was unwilling to make a choice—the result was a continuing chaotic conflict. It has been observed that less individual conflict occurs when the relationship is defined and understood.

To define communication channels. In performing a paper-flow analysis, one becomes aware of the importance of clearly defined channels of communication. One of the functions of a well-planned, well-constructed, formal organizational structure is to create an awareness of the channels of communications. Two pertinent questions are: "Who needs what information?" and "What do they do with it once they receive it?" These are simple questions, but they are not always readily answerable. Thus, a paper-flow analysis revealed that the "production manager" was tossing the production order into the trash as soon as the order was produced. Both the sales and shipping departments had been frustrated from the lack of needed information. After the source of the problems was identified and resolved, shipments were expedited and the sales department had the needed information to respond to the customer's request.

This small, independent business attempted to function without sufficient organizational planning and structure.

To define responsibility. A graphic understanding of one's sphere of responsibility facilitates the satisfaction of that responsibility. The formal planning of the organization's structure makes this possible. The individual who understands the nature and value of such a structure, i.e., has a conceptual understanding of the framework of the structure and its interaction, is able to make use of it to satisfy his/her responsibility.

Contrasting examples were found in a small independent business in
which an environment of slackness prevailed in the organizational structure. Two individuals were hired.

The first individual was employed as a sales manager. This person's background lacked depth in organizational planning and structure. As sales manager he was given a free hand, with little direction from the top, but he was unable to grasp his responsibility and failed to organize his department into a viable, effectively functioning operation. After some months of floundering, he was terminated.

The second individual, employed as a production manager came from a corporate background that utilized organizational planning and structure. He was given the same freedom as the sales manager in an environment that was as slack as the sales department. From the outset, he set forth to develop an effective organizational structure; not only did he plan an organizational structure, but he implemented it. The result was improved operating effectiveness; unresolved problems of long standing were resolved and he continued in his position. Both he and his subordinates understood their responsibilities and functioned accordingly.

To provide managerial continuity (management insurance). Many businesses are vulnerable to contingencies that result in the loss of management personnel, from whatever cause. This vulnerability is due to the lack of organizational planning, planning that would provide for management in depth and satisfy the needs of management succession.

There have been numerous cases where a business is valuable and successful today, only to be of little value tomorrow and on the road to failure due to the unfortunate loss of the owner/manager. Someone had failed to recognize the need to plan for such a contingency.

Growth of a business is inhibited or limited beyond a certain point when there is a lack of planning and development of an organization to
accommodate the managerial needs of growth.

Organizational planning and development assures management in depth and provides for management continuity. This might be considered a form of managerial insurance that assures the continuity of the business.

Cases on Organization Planning

Sound organization planning is essential in all sizes of business. Its critical nature can be seen in the following series of illustrations gleaned from the author's experiences with small business in the Southeast.

Radio Station. A radio station operated a 1000 watt A.M. daylight station and a 100,000 watt F.M. station. The station was located in a rural regional trade center. The F.M. station's market area covered a portion of three Southeastern states.

The major state university frequently conducted management training conferences around the state. These conferences/short courses ranged from 1-day to 5 different days over a period of weeks. The manager of the radio station attended a one-day conference.

One of the faculty participants discussed organizational planning and its use among small businesses. The construction and use of organization charts, complimented with job descriptions, were emphasized. It was indicated that in order to be effective, the charts and job descriptions should be related to the firm's objectives. The professor also pointed out the need to match people's attributes with the job requirements.

Some weeks later, the professor received a letter from the manager of the radio station reporting the results of changes made following the management conference. The manager first developed an organization chart and job description. He then matched people and jobs based on attributes. In the first week, sales increased 15 percent. The increase was even
more in the second week, and at the time of the letter, sales were continuing to increase.

**Lumber Company.** Easy Lumber Company is located in the center of the state. Bill, the owner, is a graduate of State University. He grew up in his father's lumber business. His father had been in the lumber business all his life. Following graduation, Bill went into partnership with his father. The firm operated two lumber mills with Bill managing one and the father the other. After a number of years of successful operation, the father and son decided to split the business. Bill was fortunate to see his business continue to grow. He kept pace with the changing technology in the lumber business which enabled him to remain competitive with the integrated mills operated by the large paper companies.

After having attended a number of management training conferences, Bill began to analyze his business and to think of the future. He wanted the business to provide for his children as they grew up.

Finally, Bill reached the point that many small/independent business owners never reach. He concluded that if his business were to continue to grow, then the day had arrived when it could no longer be a "one-man show." At this point, he called in a management-professor friend to discuss the type of organizational structure that would best serve his purpose.

In the end, Bill organized the company along functional lines taking advantage, wherever possible, of the placement of experienced specialists in the key slots. Bill did not make the error so frequently found in such an evolving environment. He avoided letting older employees by-pass the new managers. If they came to him he would send them to the new manager.

Bill has been able to see his business continue to grow and succeed where similar businesses have failed. His respect for organizational planning and development appear to have been a major key to the success he
has achieved.

**Baking Company.** The company is a family-owned and operated business producing a line of specialty products sold through fast food and vending outlets. The company is the second generation of similar businesses. The first was sold to a major national food company. Two younger family members were given management contracts as a part of the acquisition package.

The present business was originated by the father, prior to the sale of the original business. The product lines, while similar, were significantly different. The newer business was successful from the very beginning. Its products were readily accepted and enjoyed continuous growth in sales volume.

As time passed, it became apparent that the father was concerned about the future of the business. While not openly discussing his concern, to some who knew him well, it was apparent. Some two to three years, after his initial concern, the sons' management contracts were purchased by the acquisition company. One son elected to re-enter the family business. About the same time, the father developed some serious health problems. While not immediately terminal, five years later it claimed his life.

In the interim, the father gave a lot of thought to planning concerning the business' future. It involved training the son to replace him and to better organize the company's operation in order to make it more profitable. A primary objective was to achieve an income level sufficient to provide for the family's economic needs.

The success the company is enjoying today attests to the success of the organization and planning carried out in the critical period.

**Integrated Stone Fabricating Company.** This company, as is the case of many stone companies, had been a family business. However, due to death and the sale of interests by some family members, the ownership had narrowed to two family members and their children.
Historically, all aspects of the business had been profitable. The family member who was actively involved in the daily operation began to question the feasibility of continuing to operate both the quarries and the fabricating plant. Traditionally, quarrying is significantly more profitable than fabrication. In addition, the rigors of operational management are less demanding in quarrying.

The impact of this dilemma soon spilled over into the plant. The end result was the beginning of a serious labor and lower-grade management turnover problem. This brought additional concern to the chief operating officer. The decision was made to undergo a management audit. A professional was brought in to conduct the audit. The audit report made two major recommendations, based on the organization; bring in a competent individual to manage the daily operations; and, bring in another person to be financial vice-president.

These two organizational changes have resolved the labor turnover problem. In addition, the overall operating effectiveness of the company has significantly improved.

Family farm-service business. This business was a mixture of first- and second-generation family members. However, the actual direction and operation of the business was done by the eldest son. In a period of 13 years, the business had made a major turn around and had achieved a significant level of profit. The firm had initially operated as a proprietorship, but at the time the son took over it became a partnership.

Management was inadequately staffed, there was no plan for management succession, risk exposure was substantial, and the exposure to estate taxes was potentially heavy. The son acting as the chief operating officer had other interests which took him away from the business for prolonged periods. Survival required changes, but, what?
Upon the recommendations of a consulting team, the problem areas were attacked. The business was incorporated. A formal organization structure was established. A program giving depth to the management group and a plan for management succession was carried out. Plans were made related to preparation for estate tax liability. These changes made it possible for the eldest son to take on new interests and responsibilities, and left the running of the business to other family members, who were successful in their endeavors.

Chemical Compounding Company (family-owned). The company had achieved a sales level of $1,000,000 per year for a number of years. After adding outside members to its board of directors, and recovering from a financial crisis, the business began to achieve increased sales and profits. Little thought had been given to the organization structure. Actually, daily routines seemed to occupy the president's time.

Following some minor health problems, the president suddenly became concerned about retirement and plans for the future of the business. If he were not able to be there, who would run it? Since the business made up most of his assets, and his income was dependent on this source, something needed to be done. After some discussion with the board of directors, it was concluded that the outside members would function as an ad hoc executive committee.

At the outset, the committee decided to analyze the business' operation in detail, and to interview key personnel to assess the present management. This process enabled the committee to conceptualize the type of organization needed to effectively operate the business. In addition, it discovered that the president's son, a person in his middle thirties, seemed to have the potential to become the company's chief operating officer. The father, who in the past had not been on the friendliest terms with the
son, appeared pleasantly surprised that the committee had designated the son to be trained as his successor. Up to this point the son had appeared to be more errand boy than anything else. Once the recommendation was made by the committee, the father moved quickly to increase the son's responsibility. He involved the son in key discussions concerning customers, products, and operational problems. In this transition period, it was understood that the ad hoc committee would serve as a backup—a kind of managerial insurance. The change in organizational structure accompanied by long-range planning has contributed to growth in sales and increased profitability.

**Industrial equipment manufacturer.** This company was organized by a group of aero-space engineers to produce an industrial item. While there was one competing product, the new product was designed so that if a part needed repair, you would not have to replace the complete unit as was the case of the competing unit.

The principals became so engrossed in "the doing" of daily routines that little attention was given to organization planning, budgeting, or other control matters. Because of a lack of both organizational planning and matching people with appropriate skills to fill some key executive positions, the company soon discovered it was in financial difficulty. This delayed the company in gaining its rightful place in the market. In fact, it had to struggle to avoid bankruptcy. Finally, the company was able to bring in, on a regular basis, a consultant who had achieved substantial success in his own business. In time, he was able to formulate an organizational structure that moved the business from financial crisis to financial success.

3. **PLANNING FOR MANAGEMENT SUCCESSION**

A small business most commonly revolves around the management skills
of one person, the owner. As it matures, however, its survival depends upon thoughtful preparation for management succession.

**Purpose of Planning for Management Succession**

To provide for division of labor and reduced workload. Unless the organization has been developed to accommodate both management succession and a division of labor, two things seem to occur, the limits imposed by the dimension of time restrict the completion of needed tasks and the use of resources are restricted. This latter case impacts on sales volume and profit margins. The often quoted statement, "I cannot afford to hire anymore people," should be reversed: "I can't afford not to hire more people."

In planning the organization, a basic premise should be that each position should make a contribution to profit. Otherwise, the position is uneconomic and should be eliminated.

To provide for organization growth, expansion, and acquisition. The approach to this issue seems to need a positive attitude, not a negative one. The limiting factors of time and abilities preclude the opportunity to grow, expand, and acquire additional businesses. In analyzing individual businesses one discovers opportunities that would be available to the business if it possessed sufficient managerial personnel to accommodate the change.

There are instances that demonstrate the value of being able to take advantage of such opportunities when they become available. On other occasions, businesses acquire needed managerial personnel through the acquisition and consolidation process. The planning process is a major key in pursuing this route to provide the needed management personnel.

To provide for management contingencies. Major and unforeseen problems can quickly cripple a small business. Such contingencies include the following:
a. Illness. It is essential to provide management in depth to take care of the operation when unforeseen illnesses occur. On occasion, it has been observed that businesses are closed due to the illness of the owner. This not only jeopardizes the business but the owner's resources and income as well.

b. Injury. Injuries on the job or elsewhere that interfere with the owner of the business performing in his usual manner creates a crisis. If such problems are to be avoided then the needed management personnel must be in place and trained to meet the needs of the added responsibility.

c. Retirement. It is desirable to plan for retirement and develop an organization that will accommodate the event. Target dates may be developed to accommodate the phasing into retirement. However, unforeseen events may push the business owner into an earlier retirement than anticipated. If appropriate planning and implementation with organizational development has occurred, the need is met whatever the time.

d. Death. Death is a very difficult matter to deal with as a very real management contingency. The problem seems to center around these issues: the individuals who close their mind to any contemplation of death; the individual who assumes that there is still plenty of time to take care of preparing for it; and the individual, though death is certain, who has an inherent belief that he will live forever. The results of thinking in this manner have so often imposed a burden on their survivors. Others have been made aware of the importance of taking preparatory measures to establish an organization that will assure the perpetration of the business.
Problems of Planning for Management Succession

Family emotions. It is difficult to prevent family emotions from intruding into the planning process for management succession. It has been observed that the longer the time frame and the anticipated time for the management succession transition to occur, the simpler it is to carry out the planning process. Conversely, the shorter the time frame the more sentimentalities, personal jealousies, and emotions complicate the process. In some instances, it completely terminates the process, and inevitably leaves it to the court to resolve, which is a circumstance that rarely provides satisfaction to the parties involved.

"One-person show." In those businesses that have functioned around one-person's authoritarian management and control, it is very difficult to have that individual agree to plan for management succession. To plan for this kind of transition, it is essential that this authoritarian principal agree to a phasing-out process for himself and a phasing in process for a successor. So often, this individual is not prepared to adjust or to accept a lesser role.

Unwillingness to confront the uncertainty of life's contingencies. There are those entrepreneurs who play such a dominant role in the operation of their business, and whose thinking is of such a rigid nature that they are unwilling to accept that there are uncertainties whose contingencies must be confronted. Therefore, they resist the formulation of plans to resolve the issue of management succession.

Status quoism. It has been observed, that many people are much more comfortable with the known than the unknown. To plan for change, i.e., the planning for a program of management succession produces an element of uncertainty which some people are unwilling to accept. It is a formidable barrier in some people that cannot be breached.
Personal greed and selfishness. One of the more difficult obstacles to overcome in planning and implementing management succession is that of personal greed and selfishness. The individual with these characteristics develops a spirit of aggressive, defensive antagonism. It is best illustrated by the comment of the entrepreneur whose only surviving heir, besides his spouse, was a son. When told that the management succession plan need only satisfy three people. His quick retort was, "Who are they?" When told it was his wife, the son and himself, he replied, "You are wrong, only my wife and I are to be satisfied."

Belief that life on earth is eternal. Among intelligent people, it seems difficult to comprehend, that in the twentieth century that there are people who by their behavior support this idea. It is detected by their actions, their resistance to planning and making preparation for management succession and its transitory phase. These people refuse to discuss it; in fact, they appear offended when the subject is mentioned. The head of a nationally known small manufacturing company, when asked about his plans for a replacement, came back with a sharp quick response, "I plan to be around for a long time yet." For a man in his sixties, this was out of step, when so many people in industry are planning for retirement, or even early retirement.

Cases on Organization Planning and Management Succession

Family tourist business. The business had its origin in a very simple way. It evolved initially from the need of the traveling public to be fed in a remote geographic section. In the beginning, the mother prepared the meals in the family kitchen and served them in the family dining room. As roads were improved and paved, the volume of business increased. Separate structures were built to accommodate lodging and the larger number of customers
to be fed. As time passed, the second and third generation became involved. While the business grew, little formal planning for the organization, its structure, and future took place. Even so, the business grew and prospered, providing income for not only the family members but for local citizens as well. Because of the mother's age and health, her death might have been anticipated and more formal plans for management succession and the future of the business projected. However, this did not happen and for a time after her death the future of the business seemed in jeopardy because of family dissension and lack of direction. Fortunately, one of the third-generation family members was able to prevail on the other family members to agree to a consolidated plan and direction. Once this had been accomplished, the business again returned to the profitable pattern of the past.

Small potato chip business—a one-person show. The owner had initiated the business as a means of survival. He prepared the potato chips, bagged them, and delivered them to the restaurants and grocery stores who were his customers. For the scale of operation, the owner enjoyed a satisfactory level of success from the venture. On one occasion, when a friend was discussing his business with the potato chip entrepreneur, the friend asked if there were any plans for the addition of people to the potato chip business. The response was no, he liked it just like it was, that he didn't need any help. The friend responded, "What will you do if you should get sick?" The potato chip owner said, "I don't plan to get sick." Unfortunately, he did become ill at a later date. Without anyone to operate his business, he lost it.

A single-person real estate business. The business was established by the owner when he was in his early twenties. Operating in a rural county seat, he seemed to enjoy success from the beginning of the business. Having been reared on a farm, he understood the language of the farmer, so
he specialized in farm real estate. Occasionally, he did sell a "house and lot" in one of the towns of the county. During the depression years of the thirties, he did title searches and prepared abstracts to enable farmers to obtain "Federal Land Bank Loans." In this period, due to the volume of clerical work, he hired two female assistants. However, when the abstract activity subsided, he terminated the clerical assistants, reverting to his earlier sales practice.

Because of his reputation, he expanded his activities to cover a four-county area following the end of World War II. He enjoyed a comfortable income and in the "off season" was able to do all the fishing he cared to in a nearby lake. From time to time he discussed retirement, but his volume of activity continued at a level to make retirement unattractive. Then it happened—he developed arthritis in his knees. At first, he would take clients to the property and point out the property lines and let the client walk the property. In time, he could no longer drive an automobile, so he was forced to close his office and terminate a successful business—a business that could have continued if he had planned for management succession.

Soft Drink Bottling Franchises. Franchise A was located in a university town. It was one of the earliest franchises issued by a major soft drink company. In planning for the future operation of the bottling company, it was concluded that only one family member from each generation would be involved in the management of the company. Other family members would be beneficiaries of income, but otherwise would not have any involvement. Now in the third generation of the owning family, the business has made the necessary changes and grown to conform to the times.

Franchise B is located in a rural area, but the population it serves is comparable to Franchise A. The original owner of Franchise B had once had an opportunity for an additional franchise in Florida. Unable
to personally investigate the potential, a brother was sent to survey the possibilities. Upon his return, the brother reported that the territory was too infested with mosquitoes to be worth anything. To the chagrin of the third generation, some years later, that franchise was sold by the initial franchisee for thirty million dollars.

No formal plans were made for perpetuating Franchise B within the family. During the second generation it was operated by one of the two surviving heirs and that heir's spouse. Upon the death of that heir, the spouse continued to operate the company, though well past the normal retirement age. The other heir and spouse, along with their two children, were members of the Board of Directors. Each family member was paid a fee for attending quarterly board meetings.

Instead of responding to a changing market and expanding its facilities and services to meet the market requirements, the facilities were permitted to deteriorate. At this point, the family has been living off the capital for a number of years and an impasse seems to exist. Should they sell out, or should they upgrade the operation and revitalize it, and if they did this, who would manage it? Obviously, while Franchise A has and is being handsomely rewarded for its planning and accommodating of management succession, Franchise B is paying a tremendous price psychologically, as well as economically, for the lack of it.

**Small Shoe Component Manufacturer.** This company was established in an abandoned school house located in a rural area near the intersection of two state highways. The company was formed by two principals, the older was technically oriented, having spent his life in the business, and the younger was sales oriented. Actually, the existence of the business was dependent on the technical and managerial skills of the older man. Without the presence of the older man, the company could not exist. He was concerned about
this dilemma; in the back of his mind he wanted to retire sometime in the next two or three years. Yet, since all of his capital was tied up in the business, how could he afford to retire? He did not feel that he could trust his partner to learn enough of the business to effectively manage it. What was he to do? Unfortunately, he could not bring himself to a decision or to bring anyone in to replace him as manager, once they had been trained.

Small diversified business involved in construction, manufacturing, and service activities. This business had its origin while its owner was still a university student. Initially, it was a lawn care business; then, some of the lawn care customers needed some maintenance work. After that he began producing some wood products for one of his manufacturing customers. Later that customer decided to abandon one of its product lines, so he took that over. He had nothing planned initially, but he moved more like a paramecium, ingesting whatever fell in his path. Some of his activities seemed profitable, others were not, but he thought he needed those to round out his operation.

One of his great concerns was how to best allocate his time. He never seemed to be able to resolve this. Also, how to better allocate his other resources? He understood from a management viewpoint, that he was spread too thin to effectively manage all of his far-flung operations. Yet—he did not feel able to place anyone else in an upper level management position whom he could trust. In addition, there was the concern over what would happen to his businesses if he were not there to manage them?

Family owned manufacturer of farm equipment. The company was one of many small companies scattered around the country that manufacture specialized farm equipment. The basic products of this company were: peanut drying wagons, cotton wagons/trailers, and tobacco harvesting devices. The business had been started by the father, who was dominant in managing
the operation until health conditions forced his retirement. His sons had entered the business as each was ready to enter the employment stream.

Through the years no consideration had been given to the development of an organizational structure or to make provisions for management succession. Possibly, the father could not bring himself to make a selective choice or perhaps he considered that the sons would be able to manage it collectively.

Upon the father's retirement, the four sons took over the management of the company as a committee. The first year under the new setup, things seemed to go well. It was a seller's market and they were able to sell all they could produce. Then, things changed in the following year, it was no longer a seller's market, but a buyer's market. Lacking a dealer organization, the company was soon in sales difficulty. The sons were unable to evolve a solution to their dilemma and by year end, they were in serious financial difficulty. Early the following year they were forced to accept a new investor, giving away control of the business. In the end, the family completely lost the business.
1. INTRODUCTION

This paper reviews the types of transportation, and transportation services available in the region, provides some useful suggestions regarding carrier selection by small businessmen, and briefly evaluates the means of transport available in the Southeast. Increasing costs, potential energy shortages, and rapid changes in the organization and regulation of the transportation industry make it important for the small businessman to review his alternatives. In recent years, the South has been fortunate enough to see an exceptionally good transportation network develop.

2. GENERAL CARRIER TYPES, SERVICES AND PRICING

Types of Carriers

The basic types of carriers are railroads, motor carriers, air carriers and water carriers, but there are some legal distinctions within each of these that one needs to know about. These differences can affect the rate you pay, the type of service you get, and even the liability of the carrier.

Thus, carriers may be common carriers, contract carriers, private carriers and exempt carriers. In addition, there are two others that are legally classified as carriers but actually are not. These are the transportation broker and the freight forwarder and will be discussed later.
Common Carriers are those that hold themselves out to the general public for hire and may not discriminate between people, places or commodities. They are highly regulated by law and may not change rates, routes, or services without permission.

Contract Carriers, on the other hand, limit their service to those with whom they have specific contracts. They are not as highly regulated as common carriers and are usually distinguished by the specialized nature of their services and/or equipment. Examples would be a motor carrier company that carries automobiles only and a tank truck company.

Private Carriers are those that carry the products of the company that owns the vehicles. That is, the transportation service is incidental to the primary function of the company. This is called the primary business test and is used by the Interstate Commerce Commission to distinguish private carriers from other types. Only under certain narrow circumstances can a private carrier transport goods for other people for compensation. An example of a private carrier would be a carpet manufacturer who has his own fleet of trucks or a bakery that has its own vehicles for sales and delivery purposes.

Exempt Carriers are the result of specific legal provisions that allow carriers of various types to depart from normal regulatory provisions. For instance, any type of motor carrier is exempt from any type of economic (not safety) regulation when it is carrying non-processed agricultural commodities. Thus, a common motor carrier would be exempt from rate and route regulation while carrying a load of fresh green beans.

Railroads are either common or private carriers. There are relatively few miles of private railroads in this country (examples: The Aluminum Company of America, Ford Motor Company) so the overwhelming majority consists of common carriers. There are no contract railroads nor exempt railway movements.

Motor carriers may be either common, contract, private, or exempt.
Common and contract carriers are so designated by their certificates or permits which define their jurisdiction, type, and scope of operations. The primary business test and the commodity carried are used to determine private and exempt status.

Domestic inland water carriers are either common, contract, or private. The nature of river barge movements and certain exemption provisions in the law result in most inland water movements being either exempt or contract. It should also be noted that contract movements are subject to very little economic regulation.

Air carriers are not yet a major force in freight movements, particularly in smaller communities. They are designated as either common or private carriers, although provisions in the law provide for exemptions that allow common air carriers to provide charter service on a "contract" basis.

Two special cases were also mentioned above. The transportation broker, while actually not a carrier (although he might do some local pick up and delivery) is designated as one by the Interstate Commerce Commission (I.C.C.). His function as a broker is to bring the buyer and seller of transportation services together, for a commission, of course. Thus, a small motor carrier might list himself with a broker rather than hire salesmen. Likewise, a small shipper might use a transportation broker in lieu of hiring a traffic manager. It should also be noted that the transportation broker often is a warehouseman as well.

Freight forwarders exist because there is a difference between the carload (rail) or truckload and the less than carload/truckload rate. This will be discussed in more detail later, but carload and truckload rates are usually considerably less per 100 pounds than those for smaller shipments. Therefore, a freight forwarder can consolidate a number of small shipments into a carload or a truckload shipment and ship them at the lower rate. The
rate he charges the shipper will be lower than the less carload/truckload rate and somewhat higher than the CL/TL rate. The freight forwarder normally also provides break bulk and delivery services at destination. In fact, in many instances, the shipper will pay the less CL/TL rate because of the many additional services that the freight forwarder provides. The forwarders rates and services are regulated by the I.C.C. and he must have a license from it to operate. Forwarders may be either surface or air forwarders, but not both.

**Carrier Regulation**

The carriers described above, except for those which are private and exempt, are subject to varying degrees of economic regulation. This type of regulation involves control of rates and fares, schedules, routes, types of freight that can be hauled and sometimes even permission to enter or leave the business. Accounting systems are controlled, tariffs must be approved and permission is needed before two carriers can merge. Nearly every aspect of common carrier business activity is controlled to some degree.

Surface carriers, including railroads, oil pipelines, motor carriers, surface freight forwarders, and inland water carriers, are under the jurisdiction of the Interstate Commerce Commission. This eleven-member commission was created by the Interstate Commerce Act and the provisions of the Act are used by the I.C.C. to regulate the affected carriers.

Commercial air carriers are regulated by the Civil Aeronautics Board which administers the provisions of the Federal Aviation Act. This legislation not only contains the same sort of economic regulation that applies to surface carriers, but also contains comprehensive provisions concerning air traffic control and safety. These latter provisions are administered by the Federal Aviation Administration, which is in the Department of Transportation.

Recently, commercial air carriers were partially deregulated by the
Air Carrier Deregulation Act of 1978, passed in October of that year. This Act gives the carriers some rate and fare flexibility that does not require approval by the Civil Aeronautics Board and allows them to pick up unused routes if they use them within forty-five days.

Also, there is currently being considered in both Houses of Congress legislation that would substantially deregulate railroads and motor carriers. Although it is premature to speculate on the impact of such legislation until the nature of its provisions are known, it is expected that the nature and type of carrier services in the Region would not be affected.

Carrier Services

One of the most important aspects of carrier selection involves the specific types of service that are needed and whether or not the carrier offers them. Although most of these special services are more important to the shipper than the receiver, it is imperative that both parties know about them. It should also be pointed out that the service is available only if provided for in the tariff and normally there is an extra charge for it. Examples of some of the more important of these services follow.

**Diversion and Reconsignment.** A diversion is a change in the destination of a shipment while it is en route but before it has reached its destination, while a reconsignment is a change in the destination after it has reached its originally billed destination. The shipper, receiver, or owner of the goods may use these services for a number of reasons; the shipment may not have been sold until after it was en route, the order may be cancelled, or the receiver may decide to have the goods shipped to another warehouse. Specific rules applying to all aspects of reconsignment and diversion appear in the appropriate tariff along with the charges therefore, and should be consulted if this special service is desired.

**Stopoffs.** This service enables a rail car or a truck to leave the
billed destination and stop at one or more points for partial loading and unloading. Thus, a carload of stoves could leave the manufacturer and be delivered to several retailers en route to a final destination. Normally, the stopoff(s) must be for partial loading or unloading but not for both. Again, whether the service is available and the rules governing it will be found in the carrier's tariff.

**Protective Service.** This special service refers to refrigeration and heating. Mechanically refrigerated rail cars and truck trailers, ventilator type box cars and icing represent equipment which may be furnished upon request. There are also a number of types of heaters which are placed in cars to protect against cold. Again, these special services are available only when provided for in the tariff. The extra charges depend on the specific type of service requested.

**Storage.** Usually storage is thought of as applying only to less than carload or truckload shipments which are warehoused by carriers before the transportation service has begun or after it has been completed. However, under certain conditions it can also apply to carload/truckload shipments. Storage is an actual part of the transportation service only for the period of time normally required to make delivery. After this "free time" of storage in the carrier's terminal or warehouse expires, storage charges are assessed and the liability of the carrier is reduced to that of warehouseman.

**Tracing and Expediting.** Tracing involves trying to find a shipment that is delayed en route. Some carriers belong to tracing bureaus, while others may have a special department that handles this work. The most important thing to remember is that the carrier must be furnished certain basic information before it can effectively trace a shipment. The shipper or receiver should provide the following information along with his request for a tracer: shipper, origin, receiver, destination, date shipped, commodity, route, car or truck.
number, and bill of lading date and number.

Expediting refers to special handling of a shipment so that it will be delivered more promptly than usual. Most carriers offer this service and it is most successful where arrangements are made prior to the shipment. If the goods are already en route, effective expediting can occur only if the above listed tracing information is provided.

Transit Privileges. A transit privilege allows a shipment to move from origin to destination with a stop at an intermediate point where the freight is unloaded, stored, processed, reloaded and reforwarded. Actually, two separate movements are involved but they are considered as one and the advantages are apparent. Normally, the through rate is charged plus an additional "transit" charge. Of course, the storage and processing charges are extra. The availability of transit movements, the rules surrounding the movement and the charges involved will be found in the carrier's tariff.

Pickup and Delivery. Free pickup and delivery on rail less than carload movements is not normally available. Motor carriers, however, normally offer store-door to store-door service, thus giving a more complete service to shippers. Some motor carriers establish a delivery zone, outside of which there will be a charge for pickup and/or delivery. In addition, many motor carriers have established home delivery charges where residences are involved.

Weight Agreements. Weight agreements between the shipper and carrier can result in economies and reduced delivery time when reasonably accurate weights can be determined without weighing each carload of freight. Under such an arrangement, the carrier's agent will accept the weights declared by the shipper. In return, the shipper agrees to make his records available in case the carrier or his representative desire to make a subsequent check. If it is determined that undercharges do exist because the weight was understated, the shipper agrees to pay the carrier promptly.
Peddler Cars. This is a less than carload/truckload service that some carriers offer and is particularly useful to the small retailer where available. Under this arrangement, a number of small shipments can be delivered to different receivers en route. The freight rate is paid to a final destination but the shipments are distributed at various intermediate points along the way.

Pool Cars. This is a situation where the shipper combines all his less carload consignments and bills them to one receiver at one destination. This person acts as an agent for the shipper in delivering the shipments.

Package Cars. This is a scheduled expedited service that rail carriers offer in certain areas. A number of less carload shipments are loaded on the special car by the carrier and billed to the carrier's agent at the scheduled destination where they are unloaded. Some of the shipments may be held at the freight station for delivery while others may be transferred to another car for another movement. Quite often the transportation division of local Chambers of Commerce publish bulletins on package car service that is available to the community.

Carrier Selection

Who Chooses the Carrier. In the absence of any other condition, the shipper of the goods normally selects the type of carrier and the specific transportation company. This assumes, of course, that service is available to the destination in question and that the carrier also offers the type of service that is desired. The above discussion of the various types of services should be helpful in this respect and the shipper should keep the needs of the receiver in mind. This is particularly true in selecting the type of carrier. Once this has been done, other factors enter the picture. A small community may be served by only one railroad and only a few motor carriers. It might also be that only one motor carrier gives service from the supplier's city.
In such cases, it becomes a matter of convincing the carrier, or the regulatory agency, of the need for specific types of service. It might also lead to a decision to go into private carriage.

In the final analysis, however, it should be pointed out that where a choice exists, the shipper will honor the receiver's desires concerning which mode and company to use. After all, the receiver is the shipper's customer and retaining his goodwill is important in any aspect of business.

**How to Select a Carrier.** Carrier selection obviously depends on (1) the number and type of carriers serving your community, (2) the types of services they offer, and (3) the types of services you need. Surveys over the years indicate consistently that the following considerations seem to be the most important from the standpoint of most receivers; previous service rendered, types of service available, cost of service, materials handling facilities available (at both shipping and receiving stations), the financial stability of the carrier, and the claim record of the carrier.

Sometimes reciprocity is a factor in carrier selection, although it is not always considered to be a good policy. Reciprocity involves using a carrier that does business with you in some manner or who aids you (outside the transportation area) in some respect. Unless reciprocity is based on some logical, sound basis, it should be avoided as it could result in poorer service in the long run or cut you off from other carriers in times of need.

Beyond these general considerations, there are some more specific things to consider in matching the type of carriers, the commodity in question and the type of service/delivery time needed. For purposes of this discussion, we will assume that all types of transportation are available. However, we will emphasize the most likely alternatives for small shippers and receivers.

If the commodity is needed in very large quantities, has a relatively
low unit value and if time in transit is not very important, these railroads offer the lowest prices per ton per mile. Examples would be animal feed, fertilizer, grain, ore, coal, sand, gravel, etc. Since railroads for the most part no longer offer less than carload service, this means the shipment weight for one carload will vary from 10,000 to 80,000 pounds, depending on the commodity. (These are the minimum and maximum carload weights listed in the uniform freight classification).

In many instances, the railroads have closed stations in smaller communities and have set up "mobile agencies" which provide certain services to these communities. If you are involved in such a situation and receive or ship in large quantities, it would be well to contact the mobile agent in your area for rate and service information.

Motor carriers, on the other hand, are more efficient with smaller volume shipments and over intermediate to shorter distances. They can give quicker delivery time and you are more likely to get pickup and delivery service. If you are a volume shipper, you might see if there is a commodity rate on the commodity you ship or receive. It probably will be a little higher than the rail carload rate, but service should be faster.

For smaller motor carrier movements, the class rate will be related to the weight and distance. In the current class rate tariff for the South, for any given distance there is a different weight for shipments of less than 500 pounds, for 500 pounds, but less than 1,000 pounds, 1,000 but less than 2,000, 2,000 but less than 5,000, and 5,000 up to the weight specified for a truckload shipment. This latter will vary from about 10,000 to 40,000 or more. For the others, the rate per pound will be less for each weight bracket.

Since, in most cases, the rate per pound mile will be the same (assuming you decide to use a motor carrier), selection of the particular trucking company will depend on the factors mentioned above.
Unless your community is served by a commercial airport, the ground transfer cost and time will offset, in most cases, the advantages of air transportation. Emergency shipments and small shipments of high value are sometimes justified for points not served by commercial airports.

For regular or emergency small volume shipments at moderate cost, consideration should also be given to bus package express and/or United Parcel Service. The former is available to any community that has either Greyhound System or Continental Trailways System service.

3. TRANSPORTATION SERVICES AVAILABLE IN THE SOUTH

It is proper for a nation or a region to analyze its transportation facilities from time to time to determine the state and extensiveness of the physical plant, the shipping cost and transit times from supplying areas on to major markets. Such an analysis may suggest possible avenues of improvement. For maximum economic growth, any advantage enjoyed by an area because of its transport systems, should be made apparent to existing firms or to firms that may be considering a location in the area.

These eight southern states are served well by seven major Class I Railroads (The Clinchfield, Illinois Central Gulf, Florida East Coast, Louisville and Nashville, St. Louis-San Francisco Seaboard Coast Line, and Southern Railway System), all of which are in sound financial condition. These major rail carriers along with numerous short lines serve the area with over 20,000 miles of track. This amount of track gives good rail coverage for most of the region. The only major proposed abandonments of any of this track in the near future is in the State of Mississippi, where the Illinois Central Gulf proposes abandonment of some parallel track between New Orleans, Louisiana and Memphis, Tennessee. The shippers using rail transportation in the south have available to them some of the finest service and lowest rates
found anywhere in the United States.

The Interstate Highway System in the region is virtually completed. There are five North-South routes and three East-West routes. In addition to the Interstate system, most of the states have an excellent U.S. highway system reaching into the most removed areas of each state. Each state also has a secondary system, which is a feeder line complex linking rural areas and smaller communities to the primary U.S. Highway system, which, in turn, links the states to the National Interstate system.

The shippers in the region are served by an adequate number of different categories of motor carriers for hire. Common carrier by far outnumbers all other carriers for hire and by definition stands ready to serve all customers within their legal and physical capability. The shippers and receivers of freight are regularly served by a large number of local, regional, and national carriers which links the area to the nation-wide motor carrier system that furnishes good service within a minimum of transit time and at the lowest motor carrier rates in the country. While motor carriers generally have terminals in the larger cities, smaller cities and communities also have service available. The amount of service available at any particular point depends upon the economic importance of the shipper's available cargo. The common carrier generally provides some scheduled service so that shippers may be assured that shipments will be picked up daily, twice weekly or whenever needed.

For those shippers that ship large bulk shipments, the inland waterways system touches all of the states of this study. The majority of this system consist of a depth of 9 feet or more, which is capable of handling the largest tow-boats and barges.

In summary, the eight southern states of this study enjoy a very fine transportation system, entirely adequate for the present and foreseeable industrial
development needs of the area. When compared with other areas of the United States, this Southern area, has service as good as that of any other area and this service is furnished at lower cost to the shipper than in any other area of the nation.

FOOTNOTE

1. Tables of rates, routes, carrier availability, etc., to document this analysis are available from the authors at Department of Marketing and Transportation, University of Tennessee, Knoxville, Tennessee 37916.