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## Industrial Development Financing in South Dakota

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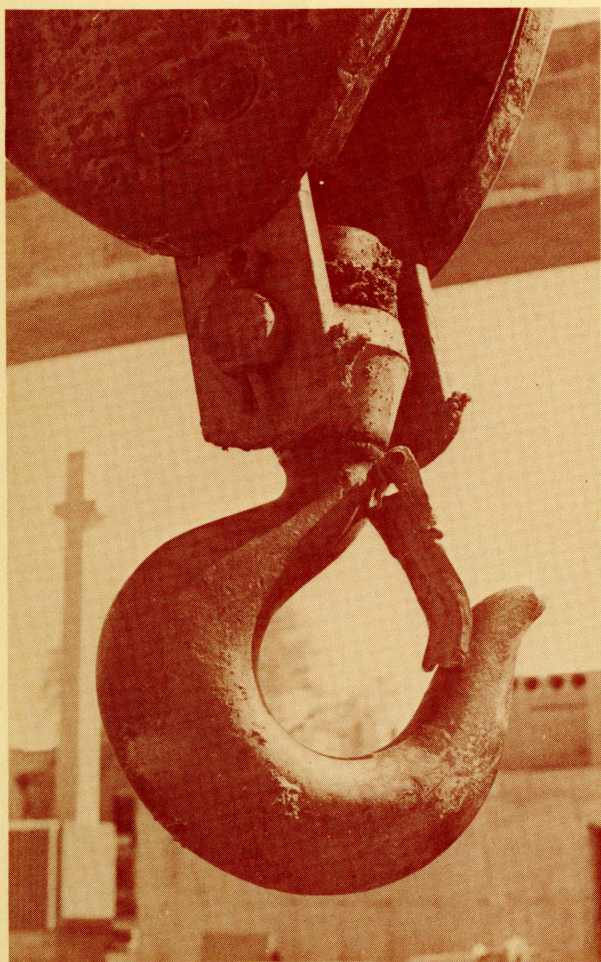
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# Industrial Development Financing in South Dakota



Economics Department  
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# Industrial Development Financing in South Dakota

Increasingly the state government of South Dakota and many of the state's communities recognize that economic diversification through industrial development must be encouraged if South Dakota is to correct such problems as low income levels and outmigration of young working people. The need to diversify is illuminated by South Dakota's relative income position and lack of employment opportunities.

In 1976, as in past years, the largest industry in South Dakota, in terms of employment and total income generated, was agriculture. Following agriculture in order of magnitude were government, wholesale and retail trade, service industries, and manufacturing.

This type of economy, where agriculture is the main export sector with the other export sectors lagging far behind, is characterized by slow growth in relation to more balanced economies, a tendency of the economy to fluctuate with agricultural cycles, and a decline in employment opportunities in agriculture.

Between 1960 and 1975 South Dakota's agricultural employment dropped from 80,000 to 52,300, a decrease of 35%. The South Dakota Department of Employment Security has projected it to drop by another 13% by 1980 (10).<sup>1</sup>

Fortunately, other sectors of the state's economy have been able to absorb most of the displaced labor. While agricultural employment decreased by 27,700 from 1960 to 1975, employment in urban non-manufacturing industries increased by 64,600, primarily in the services and government sectors. Manufacturing employment increased by only 7,900 (10).

Unless unforeseen rapid population and income growth occurs, it is unlikely that government and service industries will continue to grow at a sufficient rate to absorb agricultural outmigrants. Other sectors of the state's economy will have to absorb the workers no longer needed in agriculture, or there will continue to be outmigration from the state. Increasing employment opportunities in the manufacturing sector through industrial development is a possible answer to the problem.

Historically, South Dakota has experienced slow industrial growth. In 1970, South Dakota had new capital expenditures in manufacturing amounting to \$18.5 per person compared to \$61 per person in Montana, \$14 per person in Wyoming, \$16 per person in North Dakota, and \$108 per person as the national average (15). The same year only 7.4% of South Dakota's civilian labor force was employed in manufacturing. The national average was 25.9% (11, p. 9).

<sup>1</sup>Numbers in parentheses refer to the references cited in the Literature Cited section.

One hypothesis often used to explain the slow industrialization in South Dakota is that a shortage of financial capital for industrial development is restricting efforts to expand the manufacturing sector. The argument is made that there is insufficient capital for industrial development because either South Dakota does not generate sufficient capital internally and does not attract external capital, or sufficient capital is being generated but is flowing to more attractive investment out of the state.

Depending upon which case is true (if either), different approaches might be undertaken to alleviate the capital shortage problem. However, without a more complete understanding of the supply and demand of financial capital for industrial development, efforts to improve the economic well-being of all South Dakotans through industrial expansion will be hampered.

## Objectives

This bulletin reports results of a study of industrial development financing in South Dakota. Objectives of the study were:

1. to describe the institutions which control funds that are now or are potentially available for industrial development financing in South Dakota;<sup>2</sup>
2. to estimate the current and potential availability of industrial development funds from each source;
3. to determine by sub-state region the supplies and uses of industrial development funds in South Dakota;
4. to evaluate the current supply-demand balance for industrial development funds, and to project supplies and demands to 1980 and 1985; and
5. to identify financing sources and/or methods that might provide additional industrial capital.

## Procedure

Descriptions of the supply sources were based on information obtained from publications and from personal interviews with state supervisors of the various sources of financial capital. Included in the descriptions were legal requirements regarding the types of loans or investments each source can make, outlines of various programs available through each source, sizes of loans which can be made, and where supply sources themselves obtain funds.

Data concerning the amount of financial capital each source had furnished for industrial development projects from 1970 to 1976 were compiled from statistics supplied by each source.<sup>3</sup> Financial capital demanded was estimated by summing new capital expenditures in manufacturing for the relevant

<sup>2</sup>Note: The study does not identify funds obtained in the national money markets by parent firms located outside the state. Such funds (of unknown amounts) are included in those funds denoted personal or internal to the firm financing in this study.



years. Projections as to the availability and need for financial capital in 1980 and 1985 were made using the least squares method to fit straight lines to the time series data.

Data compiled on a state basis were broken down by planning district to illustrate the industrial activity in South Dakota on a regional basis, to determine the flows of funds among regions, and to examine the effects of such flows on capital availability in the various regions.

The estimated investment capital availability and use trends were compared to determine if a gap between supply and demand for investment capital exists now or is likely to occur in the near future.

## Sources of industrial capital

A questionnaire sent to all manufacturing and processing firms in South Dakota in the winter of 1974-1975 asked each firm to indicate where it obtains funds to finance firm establishment, expansion, and current assets; and where it plans to obtain funds for future expansion.

Responses to the questionnaire indicated that the nonpersonal supply sources currently used include commercial banks, industrial revenue bonds, Small Business Administration, Farmers Home Administration, and the Economic Development Administration. These sources and the School and Public Lands Fund are the major supply sources examined in this study.

Personal and corporate sources were not included in the study because it is virtually impossible to obtain accurate figures as to how much investment capital comes from such sources as personal friends, churches, or such internal financing methods as retained earnings, factoring, and accounts receivable. Investment capital obtained through these personal and corporate sources was estimated as the residual of the total amount of capital expended for industrial development less the amount of investment capital supplied by nonpersonal supply sources.

## South Dakota commercial banks

The most often used source of funds for industrial development is the commercial bank. In 1976 there were 158 commercial banks in South Dakota.

Commercial banks are permitted to make loans for any industrial use, provided the borrower has sufficient collateral and equity to meet charter requirements.

Two restrictions limit the amount any South Dakota bank can loan for industrial development or any other purpose.

The first, a reserve requirement, limits the total dollar amount of loans any bank can make to a specified percentage of that bank's total deposits. The required reserve percentage is determined by the Federal Reserve for its member banks and by the state for non-member banks. Bank reserves may be increased either by converting other assets to cash,

or by new deposits of outside funds. On the basis of the additional reserves new loans can be made.

The second restriction limits the amount a bank may loan any one borrower. The maximum loan a state bank can make to a single person, partnership, or corporation is 20% of the bank's capital and surplus. The maximum for national banks is 10% of capital and surplus. Although overlining to correspondent banks is common, this restriction does make banks a more likely lending source for small businesses and for firms needing funds for current assets than for large firms and those seeking capital investment financing.

Within the restrictions outlined above, whether or not a bank makes funds available for industrial development largely depends on the lending attitude of each individual banker. This attitude appears to be conservative in South Dakota.<sup>4</sup> However, banks are still the primary lending source for most firms seeking industrial development funds in the state.

## Industrial revenue bonds

A source of funds which is becoming more widely used in South Dakota for financing industrial development is the industrial revenue bond.

Industrial revenue bonds may be issued by local governmental units to finance the construction of buildings for industrial purposes and to purchase land to be used as industrial sites. The sites or buildings are then leased to private firms which pay rentals sufficient to cover the principal and interest of the bond and the maintenance of the facility.

Revenue bonds are not obligations of the governmental unit issuing them. They are secured only by the property acquired with the proceeds of the bond sale and the income produced under terms of the lease contract, and are retired only by the revenues obtained through the leasing agreement and not with public tax dollars.

Another attractive feature of these bonds is that they are subject to no legal debt limit, since they are not governmental obligations. The amount of bonds issued must still be within limits set by their salability in the bond market.

The interest rate on industrial revenue bonds depends on the bond rating of the firm being financed rather than on the rating of the borrowing municipality. A low rating of a firm would mean a higher interest rate must be offered in order to attract bond buyers.

Originally, all interest earned on industrial revenue bonds was tax exempt. However, this was changed for some new issues when, in 1968, Congress decided to allow tax-free interest only on those issues of under \$5 million (6, p. 6).

Industrial revenue bonds are allowed at the local level in all but seven states and the District of Columbia. The South Dakota legislature authorized the use of industrial revenue bonds by any municipality in 1964 (South Dakota Laws, 9-54-2). Later, changes were made in the law to allow counties and special water districts to use industrial revenue bonds (South Dakota Laws, 9-54-10).

<sup>3</sup>This data interval was selected primarily because several of the major sources being studied were first used within the last few years. Also, prior to 1970, data on new capital expenditures were not restricted to new capital expenditures in manufacturing, as were the data from 1970 to 1976. A third factor was the subjective judgment that data covering the past few years would be more indicative of the current industrial development potential and mood in South Dakota than would data from earlier years.

<sup>4</sup>In 1974, South Dakota banks with less than \$10 million in total deposits had an average loan-to-deposit ratio of 0.53 (11, p. 93). The ratio for larger banks ranged from 0.61 for banks with from \$10 to \$20 million in deposits to 0.71 for banks with over \$100 million in deposits. In the same year, banks subject to the most stringent reserve requirements of the Federal Reserve Board were allowed a loan-to-deposit ratio of 0.78; most South Dakota banks could have legally made loans amounting to about 85% of deposits.



Since the facility financed by industrial revenue bonds is municipally owned and thus is not subject to municipal property taxes, South Dakota has also ruled that payments in lieu of taxes may be negotiated with the firm leasing the facility (6, p. 7). Under this provision a few years of tax relief are usually allowed before payments in lieu of taxes have to be made. From 1970 to 1976, there were 24 industrial revenue bond issues in South Dakota, and all but four of these issues included tax relief for periods ranging from 2 to 20 years.

A drawback to the use of industrial revenue bonds for industrial development purposes is the minimum amount which can be raised without the cost of issuing the bonds becoming too high—estimated to be about \$350,000.<sup>5</sup>

Although bond issued of less than \$350,000 can be made, small industries would probably not use this method of finance. They could not or would not want to pay the high cost or the high rate of interest which would be expected because of the low bond ratings usually given to small firms.

### Small Business Administration

The Small Business Administration (SBA) was created by Congress in 1953 to help small businesses so that they could contribute to the economic growth of the country.<sup>6</sup> At that time a permanent revolving fund was established to finance the SBA loan programs. In 1966 this revolving fund was divided in two: a Business Loan and Investment Fund and a Disaster Loan Fund. In addition to the revolving funds, additional capital appropriations can be authorized by Congress. In lieu of appropriations, additional capital may be provided by the sale of participation certificates in loan pools.

To qualify for SBA assistance a small business's receipts or employment must fit into certain defined categories. To be eligible a manufacturing firm can employ a maximum of 250 to 1,500 persons, depending on the industry. Wholesale, retail, service, and construction firms are judged according to receipts.

The SBA has many programs available through which a small business may obtain financial or other assistance. The program which is most important to this study is the business loan program through which loan guarantees are provided for business construction or expansion, purchase of capital assets, or for working capital. Included in the business loan program are:

1. Direct loans of up to \$100,000. Also participation loans whereby the SBA and a private lending institution each put up part of the funds with the SBA's share not to exceed \$150,000. The maximum interest on the SBA share was 6% in 1976.
2. Loan guarantee plans through which the SBA can guarantee up to 90% or \$350,000, whichever is less, of a bank loan to a small firm. The interest is set by the bank.
3. Pool loans to corporations formed and capitalized by groups of small business companies for purchasing materials to be used in their businesses. The SBA, alone or with a bank, may lend as much as \$250,000 for each pool

<sup>5</sup>Statement by Robert Martin, Department of Economic and Tourism Development, Industrial Division, Pierre, South Dakota, June, 1975.

<sup>6</sup>Information for this section is based on the Small Business Administration's *SBA - What it is . . . What it does* (9).

member. The SBA interest is 6%, and maturity is up to 10 years, or 20 years if for construction purposes.

4. Economic opportunity loans to disadvantaged persons who desire to own their own business. A disadvantaged person is one in the low income category or someone who has been denied adequate finances through normal lending institutions due to social or economic reasons. The maximum loan is \$50,000 with maturity up to 15 years. Interest on this type of loan is 7%.
5. Handicapped assistance loans to nonprofit organizations which employ not less than 75% handicapped personnel, or to handicapped persons who operate or wish to establish a business.

The SBA also has two lending programs designed to assist development companies. One program lends money to state development companies so that they can supply long-term loans and equity capital to small businesses. The SBA may lend these companies an amount equal to their total outstanding borrowing from all other sources, with a maturity of up to 20 years, at variable interest rates. In 1976 South Dakota did not have a state development corporation.

The other program involves local development corporations. To be eligible for these loans private concerns must put up a reasonable share of the cost of a project, usually 20%. The development corporation may be organized as a profit or nonprofit corporation and must have a minimum of 25 stockholders or members. A maximum of \$350,000 may be borrowed from the SBA for each small business to be assisted, with a loan maturity of up to 25 years. The SBA participates with banks, insurance companies, pension fund groups, state authorities, commissions, and others when making loans to local development corporations.

The SBA also has a lease guarantee program for small businesses unable to lease good locations because they do not have top credit ratings. In these cases the SBA will guarantee the payment of the lease so that these businesses may obtain good locations. The guarantee may extend to 20 years on a participatory or direct basis.

The SBA also helps finance small firms through privately owned Small Business Investment Companies (SBIC's). SBIC's are SBA-licensed companies which supply venture capital and long-term financing to small firms. The SBIC's must operate within SBA regulations, but their transactions with firms are not subject to SBA approval.

Initial minimum private investment in an SBIC may vary from \$150,000 to as much as \$1,000,000. SBA may make loans or guarantee 100% of the loans made by private lending institutions to SBIC's to add to their funds for financing small firms. The maximum loan the SBA will make to an SBIC is \$15 million or twice the SBIC's private paid-in capital and surplus, whichever is smaller, and the term of the loan may be up to 15 years. SBIC's specializing in venture capital financing which are capitalized at \$500,000 or more may qualify for SBA direct or guaranteed loans aggregating up to \$20 million. In 1976 there were no SBIC's organized in South Dakota to take advantage of this program.

### Farmers Home Administration

The Farmers Home Administration (FmHA) was authorized by the Rural Development Act of 1972 to



provide credit for business and industry.<sup>7</sup> Funding for this program is appropriated by the federal government. The means by which these funds are channeled to businesses and industries are loan guarantees and direct loans.

Loan guarantees make credit available to private organizations or persons from private lending institutions with the FmHA guaranteeing up to 90% of the loan in case the borrower defaults. The private lender is responsible for writing and servicing the loan, and is also responsible for setting the interest rate.

Those eligible for direct FmHA loans include individuals, public and private organizations, and federally recognized Indian tribal units. Direct loans are obtained through application to the FmHA which writes and services the loan. The maximum repayment schedule for direct loans is 30 years for land and buildings, 15 years for machinery or equipment, and 7 years for working capital. The interest rate on these loans to private firms was 10.75% in fiscal year 1977. Public and non-profit borrowers paid 5%.

The Rural Development Act of 1972 also authorized the FmHA to make grants to rural areas or to cities with populations of 50,000 or less. The grants are to be used for financing industrial sites, including such costs as purchasing and developing land; and constructing access roads, parking areas, and utility and service extensions. Only public bodies are eligible for these grants.

The program through which the FmHA makes funds available for non-farm industries is quite a recent development. It is difficult to say what impact it will have on industrial development in South Dakota.

Since the program will be used mainly for cases which exceed the SBA loan limit, you could speculate that the FmHA will not become a major source of investment capital. Nevertheless, the FmHA loan guarantees and direct loans do provide an additional source of funds to assist in the financing of industrial development in South Dakota.

### **Economic Development Administration**

The Economic Development Administration (EDA) is an agency of the U.S. Department of Commerce, authorized by the Public Works and Economic Development Act of 1965 (18). The purpose of the EDA is to make funds available so jobs can be created in communities and areas suffering high unemployment or low family incomes. EDA programs include public works grants and loans, business development loans, technical assistance, planning grants, and research grants and contracts. Although all of these programs are helpful to industrial development, only the business development loan program is pertinent to this study.

The business development program offers assistance through direct loans or loan guarantees to finance fixed assets and working capital. Guarantees of rental payments for fixed asset leases from qualified lessors also are authorized. To be eligible for this assistance a business must be located in a designated EDA redevelopment area or economic development district.<sup>8</sup> Figure 1 is a map of these areas in South Dakota.

<sup>7</sup>Information for this section is based on the USDA, FmHA Fact Sheets "Business and industrial loans" and "Grants to help develop private business enterprises." (13, 14).

Applicants for EDA business loans may include business enterprises; nonprofit organizations; the state or any political subdivision of the state; Indian tribes; and private lending institutions including commercial banks, savings and loan associations, insurance companies, factoring companies, investment banks, and venture capital investment companies (19).

Although there is no limitation on the amount that EDA may lend any applicant, EDA funding is subject to budgetary discretions, so the general guideline is to lend not more than \$10,000 per job created or saved.

Other limitations also apply to the EDA business development program. The amount of funds which the EDA can supply for direct fixed asset loans is limited to 65% of the total cost of the fixed asset, but working capital loans may be made for the full amount required. Guarantees on loans or leases may not exceed 90% of the obligation. The limit on the length of EDA business development assistance is 25 years except for working capital loans which are limited to 5 years, and leases on fixed assets are limited to the useful life of the fixed asset.

The interest rate on EDA loans is determined by the cost of government borrowing, but is usually below the commercial bank prime rate. The equity requirement for all EDA projects is at least 15% of the total project costs. One other requirement is a technical and economic feasibility study to be provided to EDA by the applicant at his expense (19).

### **School and Public Lands Fund**

The School and Public Lands Fund is currently the only source of state money which is available for industrial development purposes.

The Office of School and Public Lands obtains its funds through the sale or rental of state owned lands. This money, held as a permanent fund, can be invested in bonds of the United States; securities guaranteed by the Veterans Administration, Farmers Home Administration, Federal Housing Administration, or the Small Business Administration; general obligation bonds of the state of South Dakota, any public school corporation, organized county, or incorporated city within South Dakota; and loans made under the Federal Higher Education Act of 1965 (South Dakota Laws, 5-10-18).

Prior to 1970, none of the School and Public Lands Fund was invested in development activities in South Dakota because the original law did not allow investments in federal government guaranteed securities. Amendments to the law in 1969 and 1970 authorized purchase of these securities.

The process by which money from the permanent school fund becomes available for development purposes is somewhat difficult for the firm trying to obtain capital.

The firm must be able to convince the lending agency (usually a bank), the guaranteeing agency (usually the SBA or FmHA), and the directors of School and Public Lands that the project proposed for funding is worthwhile. The three financing par-

<sup>8</sup>Designation as an EDA "Qualified Area" within which assistance for business development is available entails: 1) certification by the U.S. Department of Labor that the area (usually a county or, in South Dakota, Indian reservation) is eligible by unemployment and/or income criteria; 2) preparation of an areawide development plan by the local government of the area involved—or adherence by the local government to a plan prepared by the economic development district within which the area lies; and 3) designation by the EDA.



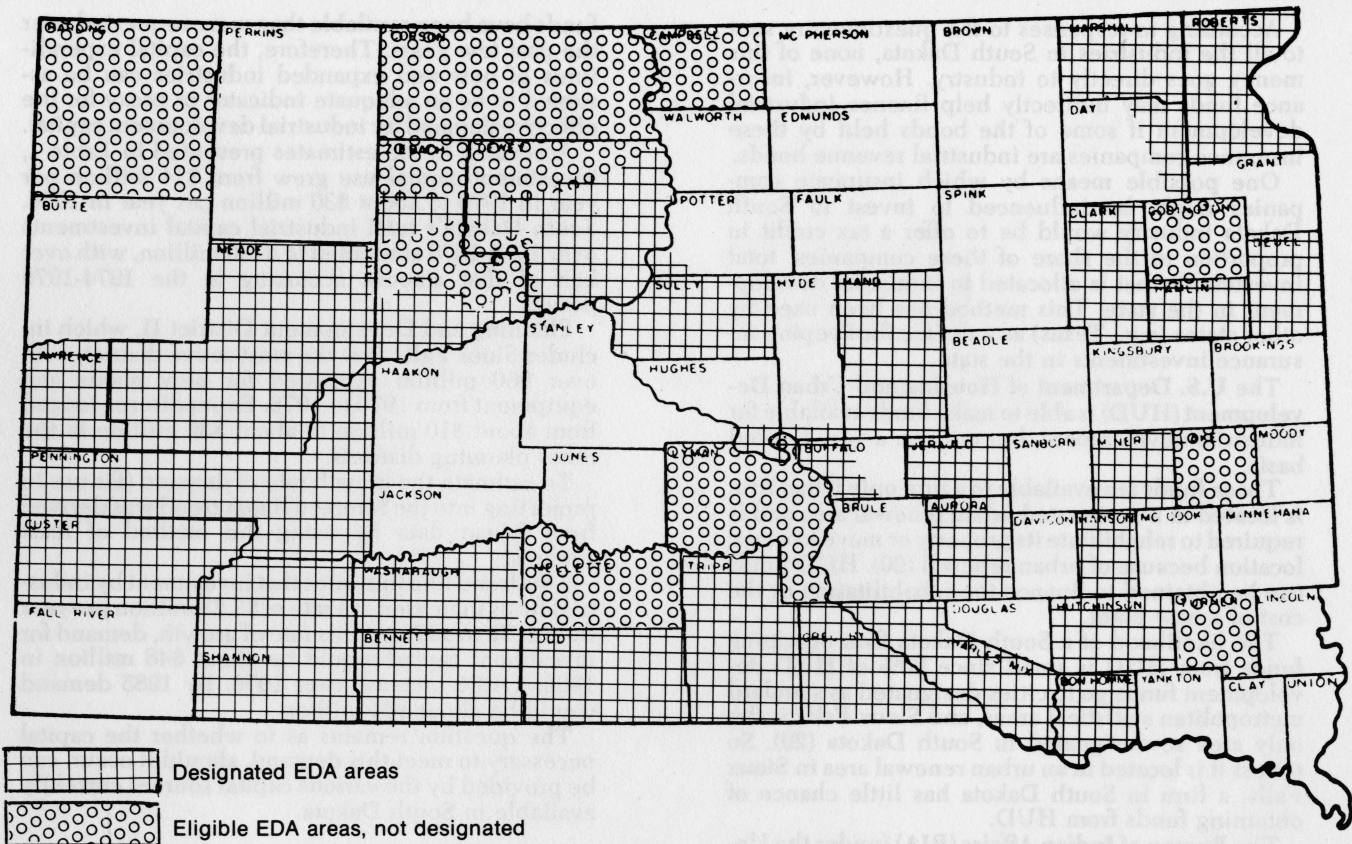


Figure 1. EDA qualified areas in South Dakota, March 1977.  
 Source: Unpublished list provided by the Denver Regional Office of the EDA.

ties will be in close contact with each other to be sure that the various provisions of the loan are being met.

Once the directors of the School and Public Lands Fund make a commitment of funds, the bank can write the loan with a SBA or FmHA guarantee. Money from the permanent fund is used to purchase the loan from the bank. The loan must be 100% guaranteed before funds from the permanent fund can be used.

Although this source of funding for industrial development is now supplying only a small part of industrial capital financing in South Dakota, it has important potential. Also, it is an example of the potential for use of state money to assist development while allowing interest earnings at the same time.

**Other potential sources**

The institutions whose activities are outlined above are the sources of investment capital indicated on the replies to the questionnaire sent to South Dakota industries. Among other sources not listed that could supply industrial development funds in South Dakota are local development corporations, the Department of Housing and Urban Development, South Dakota based insurance companies, and the Bureau of Indian Affairs.

**Local development corporations (LDC's)**, usually formed by independent groups of private citizens, are able to supply capital to industrial firms. While they are usually heavily involved with the public relations aspect of industrial development, they sometimes buy and hold land for industrial de-

velopment. They do this so that, among other reasons, new industries are not forced to pay the higher price that land speculators may charge.

The amount of capital controlled by most LDC's is not sufficient to finance the construction of most industrial facilities. Their primary financial role is to assist firms in obtaining financing from other sources, usually commercial banks and the SBA.

If the funds go directly to the LDC, they can make arrangements to construct a building for lease to a firm. Alternatively, they can loan funds directly to the firm and allow the firm to construct the building.

Profit making LDC's obtain funds by selling stock. Those that are non-profit obtain funds through dues, assessments, and other contributions. South Dakota laws allow municipalities and counties to appropriate tax dollars to non-profit LDC's for the purpose of promoting the city or county (South Dakota Laws, 9-12-1, 7-18-11). A city can levy a tax of up to one mill each year on each dollar of taxable property, and a county can levy a tax of up to one-eighth mill.

Because of the large amount of money controlled by the 74 South Dakota based insurance companies, the insurance industry might be considered a potential source of funds for industrial development. These insurance companies had approximately \$12.5 million invested in South Dakota in the form of real estate, stocks, and bonds in 1974.<sup>9</sup>

<sup>9</sup>Data based on Insurance Commissioner's work sheets for the annual report, December 31, 1974, Pierre, SD. (Because of a changed format for this report, data for more recent years are not available.)



According to responses to the questionnaire sent to all the industries in South Dakota, none of this money goes directly to industry. However, insurance funds may indirectly help finance industrial development if some of the bonds held by these insurance companies are industrial revenue bonds.

One possible means by which insurance companies might be influenced to invest in South Dakota industry would be to offer a tax credit in proportion to the share of these companies' total investments that is allocated to industrial development in the state. This method has been used by other states (e.g., Texas) as a device for keeping insurance investments in the state.

The U.S. Department of Housing and Urban Development (HUD) is able to make funds available for industrial development, but only on a very limited basis.

These funds are available to a firm only if that firm is located in a designated urban renewal area and is required to rehabilitate its property or move to a new location because of urban renewal (20). HUD funds can be obtained to finance the rehabilitation or the cost of a new plant.

The likelihood of a South Dakota firm obtaining funds from HUD is small since 80% of HUD development funds go to cities designated as standard metropolitan statistical areas, and Sioux Falls is the only area so designated in South Dakota (20). So unless it is located in an urban renewal area in Sioux Falls, a firm in South Dakota has little chance of obtaining funds from HUD.

The Bureau of Indian Affairs (BIA) (under the United States Department of Interior) is authorized to provide loans for Indian economic, social, industrial, and tourism development.

Prior to 1974 three revolving loan funds provided loans to Indians. The Indian Financing Act of 1974 consolidated those three funds into one fund administered by the Secretary of the Interior, and authorized an additional \$50 million be appropriated to the fund (Public Law 93-262, U.S. Congress, 88th Congress, 1974).

The Act established a loan guarantee program which can guarantee up to 90% of a loan made to private Indian organizations or individuals. A grant program also included in the Act authorized federal grants of up to \$50,000 per business to aid small Indian businesses.

## Industrial capital demand and supply

Before assessing whether or to what extent inadequate financing affects industrial development in South Dakota, it is important that both the demand and supply of investment capital be considered. The purpose of this section is to inventory and appraise the past and projected magnitudes of investment funds demanded and supplied for industrial development in South Dakota.

### Demand for industrial capital

The first step in the analysis of the supply and demand of industrial development capital was to determine the magnitude of the demand for these funds. The data used to estimate demand were the capital expenditures of new and expanded industries in South Dakota (Table 1).

Although these data represent only the demands that have been met; commercial banks, the SBA and FmHA, and the Office of School and Public Lands indicated in response to our questions that more

funds have been available than were requested over the past few years. Therefore, the capital expenditures of new and expanded industries can be assumed to be an adequate indicator or proxy for the effective demand for industrial development capital.

According to the estimates presented in Table 1, investment capital use grew from \$14 million per year in 1970 to about \$30 million per year in 1976. South Dakota's total industrial capital investments over 1970-1976 amounted to \$180 million, with over half of that amount occurring in the 1974-1976 period.

Planning and Development District II, which includes Sioux Falls, was the most active district, with over \$60 million expended for new plants and equipment from 1970 to 1976. Expenditures ranged from about \$10 million to about \$32 million in the other planning districts.

To estimate the growth rate of demand (for use in projecting into the future) a linear trend was derived from 7-year data by using the method of least squares.

This trend line indicates that investment by industrial firms increased at a rate of \$3.23 million per year from 1970 to 1976. At this rate of growth, demand for investment capital would be about \$48 million in 1980, a 40% increase over 1976. By 1985 demand would be about \$64 million.

The question remains as to whether the capital necessary to meet this demand, should it occur, can be provided by the various capital sources currently available in South Dakota.

Table 1. Industrial capital expenditures in South Dakota, 1970-1976<sup>1</sup>

	Planning district						Total
	I	II	III	IV	V	VI	
	\$ millions						
1970	1.60	2.24	0.58	3.03	0.41	5.90	14.03
1971	2.15	2.47	2.92	2.63	2.28	2.28	14.73
1972	1.74	11.24	2.30	3.55	1.28	1.49	21.60
1973	8.98	12.56	4.94	3.45	1.09	5.20	36.22
1974	2.96	12.72	7.19	2.99	2.11	2.01	29.98
1975	6.60	10.07	0.86	7.98	2.32	8.24	36.08
1976	7.20	8.84	1.95	1.79	0.90	6.44	27.12
Total	29.21	60.14	21.01	25.42	10.39	31.56	179.76

Source: Unpublished data supplied by the Department of Economic and Tourism Development, Industrial Division (Sioux Falls, SD).

<sup>1</sup>Note that capital expenditures by public utilities, e.g., power, water supply and telephone companies, are not considered to be "industrial" for purposes of this study.

## Supply of industrial capital

### Commercial banks

Commercial banks comprise the main source of industrial capital in South Dakota. Because exact data were not available as to the amount of industrial capital supplied by banks, estimates were obtained through use of an allocation formula with total bank commercial and industrial loans made in the state as the base data series. In a study by Loren Tauer it was estimated that 46% of the value of these types of loans in South Dakota are for industrial purposes (11, p. 63).

Industrial loans for fixed capital, as opposed to those for working capital, were estimated by assuming that the proportion of industrial loans that goes to finance fixed capital is 50%. This assumption also relied on estimates made by Tauer.

According to Tauer's study, 64% of bank industrial loans have a duration of one year or more (11, p. 64). Usually loans for fixed capital are for over one year, while most loans for working capital are for one year



or less. Adjusting the 64% to take account of loans for working capital which may be for over one year suggested 50% as an approximation of the proportion of industrial loans going to finance fixed capital.<sup>10</sup>

Commercial banks made industrial loans amounting to \$61 million between 1970 and 1976. The rate of increase of bank industrial loans was \$1.47 million per year during this period.

Projections using this rate indicate that by 1980 banks would be supplying about \$19 million for capital investments, an increase of about 67% over 1975. By 1985 about \$26 million would be supplied by banks, at the current rate of expansion.

The potential amount of investment capital supplied by banks could be greater than these projections.

As pointed out by Tauer, more rapid increases in industrial loans by banks could be affected through such means as an increase in the loan-to-deposit ratio of the banks, increased use of the Federal Reserve's seasonal borrowing privilege, an increase in the rate of growth of deposits, or by a state industrial loan guarantee (11, p. 102).

#### Industrial revenue bonds

Industrial revenue bonds (IRB's), first used in South Dakota in 1969, already are the second most important nonpersonal source of capital for industrial development purposes.

A principle advantage of these bonds is that they can finance industrial developments that are too large for banks or the SBA to handle.

Between 1970 and 1976, IRB's supplied about \$34 million of industrial capital in South Dakota. The linear rate of increase of industrial revenue bond issues was \$320,000 per year. With continued expansion at this rate, by 1980 IRB's would supply about \$7 million for investment capital. By 1985 industrial revenue bonds would be supplying about \$8.6 million.

It is likely that these projections underestimate the potential and probable rate of growth of IRB financing for industry. Several investment bankers contacted indicated that virtually unlimited funds (relative to projected needs by South Dakota industry) are available. Moreover, revenue bond issues approved or being processed in several South Dakota communities in the first half of 1977, when completed, will total more than twice the amount projected for 1985.

A factor which may restrict the use of IRB's is that municipalities may become reluctant to issue them for fear that interest rates on other municipal issues may be forced up by competition for bond market funds.

#### Small Business Administration

The Small Business Administration (SBA) is the major source of federal funds for industrial development. Most of the SBA assistance to industries comes through loan guarantees. These guarantees accounted for approximately \$11.0 million, 65%, of SBA assistance to industrial development in South Dakota between 1970 and 1976. Direct loans accounted for \$7.15 million of the SBA assistance. With a continuation of the 1970-1976 trend, total SBA assistance could decrease at a rate of \$26,000 per year, amounting to only \$2.4 million in 1980.

When assessing future SBA financing, it should be borne in mind that the SBA is more political than are several of the other sources considered; hence, funding levels and loan practices may change substantially with changing federal administrations. The same is true for FmHA and HUD. With the same assumptions direct SBA financing would be decreasing at a rate of \$63,000 per year.

Comparison of the Sioux Falls SBA office delinquency rate of 4.35% with the national average delinquency rate of 9%, would seem to indicate a conservative attitude by the SBA in South Dakota.<sup>11</sup> However, SBA officials say that any firm or development group that has come to the SBA needing financial assistance and meeting SBA requirements has been able to obtain it through the help of the SBA.<sup>12</sup>

The SBA officials contend that the SBA is underutilized in South Dakota and that more money is available than is being requested. Thus, the SBA's potential as a source of supply for investment capital may possibly be much greater than linear projections indicate.

#### State funds (school and public lands)

Between 1971 and 1976 South Dakota's School and Public Lands Office loaned \$7.8 million for industrial development purposes in South Dakota. Continuation of the 1971 to 1976 rate of increase, \$556,000 per year, would entail loans of about \$5.5 million in 1980 and approximately \$8.3 million per year by 1985.

In April 1977 the School and Public Lands Fund contained \$70 million of investments which included government bonds; federally guaranteed loans; and general obligation bonds of the state and of public schools, organized counties and incorporated cities within South Dakota. Of this \$70 million, approximately \$15 million went to industrial and commercial ventures in the form of federally guaranteed loans.

According to the office of the Commissioner of School and Public Lands it would have been possible to loan an additional \$10-12 million of this permanent fund for federally insured industrial development ventures in South Dakota in 1977.<sup>13</sup>

#### Farmers Home Administration and the Economic Development Administration

Although the SBA is the main source of federal assistance for industrial development, the FmHA and the EDA are also authorized to provide loans and loan guarantees for industrial purposes.

The program through which the FmHA loans money or guarantees loans by other institutions was started in 1974. In the program's first year of operation in South Dakota, \$180,000 was loaned for industrial development purposes and \$1.19 million of industrial loans were guaranteed. In fiscal year 1975 the FmHA guaranteed loans of \$1.12 million and made no direct loans for industrial development in the state.<sup>14</sup>

The EDA, which has been in operation since 1965, has supplied only \$520,000, all in 1970, for industrial development in South Dakota (18). Based on past experience one might rate the EDA as a very minor

<sup>10</sup>Jane Bodmer, bank examiner, office of the Regional Administrator of National Banks, Minneapolis, MN, and Van Fishback, Vice President of First National Bank, Brookings, SD, were questioned as to the validity of this assumption, and both considered it to be a reasonable approximation.

<sup>11</sup>Percentages furnished by Small Business Administration, Sioux Falls, SD.  
<sup>12</sup>Statement of Gerald Bruget, Small Business Administration, Sioux Falls, SD, in a telephone interview, May 19, 1977.

<sup>13</sup>Statement by George Kane, Commissioner of School and Public Lands, Pierre, SD, in a phone interview, May 19, 1977.

<sup>14</sup>Data supplied by Farmers Home Administration, Huron, SD.



potential source of capital, but as with the SBA and FmHA the potential amount of capital could be quite large or none at all depending on legislative appropriations.

**Comparison of supply and demand**

Table 2 and Figure 2 summarize the yearly breakdown of total capital investment financed by the six nonpersonal supply sources studied. Commercial banks are the main supply source, financing 34% of the 1970-1976 total investment of \$180 million. Industrial revenue bonds were next in importance, supplying 18.6%. The SBA supplied 4.0%, School and Public Lands 4.4%, FmHA 0.1%, and EDA 0.3% of the total. Together these sources provided 61.4% of the 7-year capital investment total, leaving 38.6% to be supplied through personal finances or through internal financing by firms.

Despite high year-to-year variability, the trend in the percentage of industrial capital investments financed by nonpersonal sources was positive from

1970 to 1976; it increased at a compound rate of about 2% per year. Thus, although the projected levels of industrial capital expenditures might require increased absolute levels of financing from personal or internal to the firm sources, the projected nonpersonal financing would supply a steadily increasing percentage of the total industrial financial capital needed.

With continued expansion of the South Dakota economy—which is an implicit assumption of the industrial investment projections—there should be no shortage of investment capital from either personal or nonpersonal sources, with the relative burden on personal financing becoming progressively less.

Projections of industrial investment to 1980 and 1985 based on the 1970 to 1976 trends are \$48.5 million for 1980 and \$64.4 million for 1985 (Figure 3). Similar projections for capital supplied indicate that, with a continuation of current trends, industrial capital available from nonpersonal sources would be

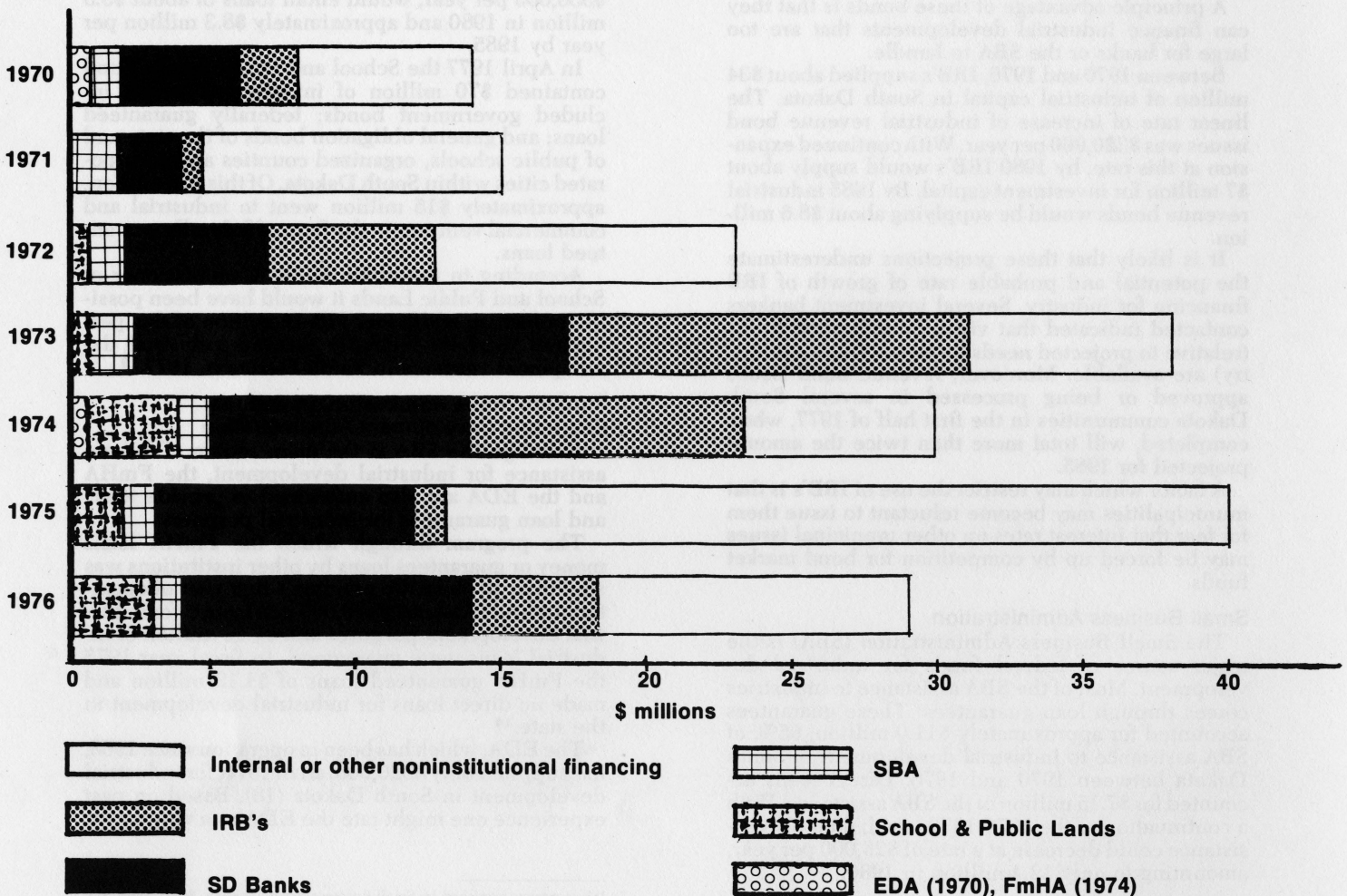


Figure 2. Sources of industrial financial capital in South Dakota, 1970-1976



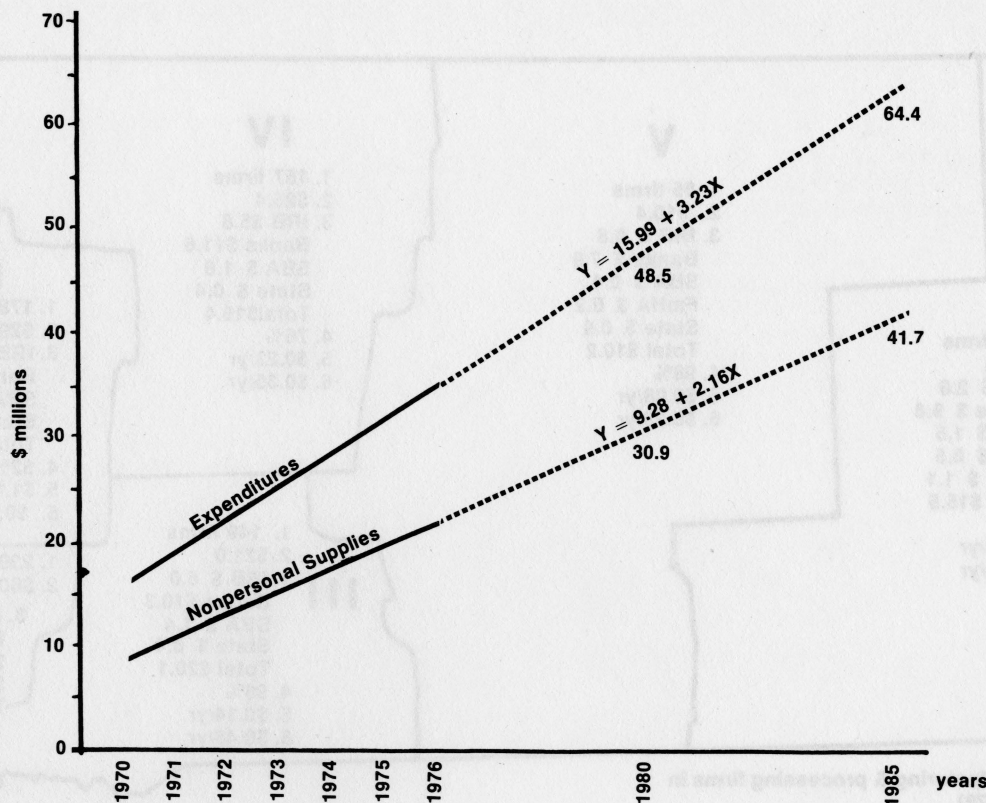


Figure 3. Comparison of new industrial capital expenditure and nonpersonal capital supply trends, 1970-1976; and projections to 1980 and 1985.

Table 2. Industrial capital expenditures compared to nonpersonal supply of industrial capital in South Dakota, 1970-1976<sup>1</sup>

	1970	1971	1972	1973	1974	1975	1976	Total
<b>Capital expenditures</b>	14.30	14.73	21.60	36.22	29.98	36.08	27.12	179.76
<b>Nonpersonal financing</b>								
SD banks	4.57 (32.6)	2.06 (14.0)	5.48 (25.4)	17.03 (47.0)	10.78 (35.9)	9.76 (27.0)	11.38 (42.0)	61.06 (34.0)
IRB's	1.85 (13.2)	0.35 (2.4)	5.65 (26.2)	12.92 (35.7)	8.40 (28.0)	0.62 (1.7)	3.75 (13.8)	33.54 (18.6)
SBA	0.51 (3.6)	1.90 (12.9)	1.11 (5.1)	1.14 (3.1)	0.88 (2.9)	1.03 (2.8)	0.58 (2.1)	7.15 (4.0)
School & Public Lands	0 (0.3)	0.04 (0.3)	0.18 (0.8)	0.32 (0.9)	3.21 (10.7)	1.66 (4.6)	2.46 (9.1)	7.87 (4.4)
Other	0.52 <sup>2</sup> (3.7)	0	0	0	0.18 <sup>3</sup> (0.6)	0	0	0.70 (0.4)
<b>Total</b>	7.45 (53.1)	4.35 (29.5)	12.42 (57.5)	31.41 (86.7)	23.45 (78.2)	13.07 (36.2)	18.17 (67.0)	110.32 (61.4)

<sup>1</sup>The percentage of capital expenditures financed by each source is given in parentheses.

<sup>2</sup>EDA

<sup>3</sup>FmHA

Sources: FDIC Assets, Liabilities and Capital Accounts, 1970-1976 editions; unpublished information provided by the lending agencies.

\$30.9 million in 1980 and \$41.7 million in 1985. Sixty-five percent of industrial capital needs would be met from nonpersonal sources in 1985. This is 4% more than the 1970-1976 average.

#### Industrial activity and financing by planning district

To further illustrate the demand and supply picture for industrial development capital, Figure 4 shows differences in the regional industrial activity in South Dakota. Information provided includes number of firms, new capital investments, amount of capital supplied from nonpersonal sources, and the growth rates of capital investments and supply of capital.

An interesting point illustrated in Figure 4 is the percent of new capital investment obtained from nonpersonal supply sources. Districts III, IV, and V had 96, 76, and 98%, respectively, of their investment capital supplied by these sources; while only 52% in District I, 51% in District II, and 50% in District II, and 50% in District VI were supplied by these sources.

This may indicate that personal and corporate finances are more important in Districts I, II, and VI, or it may be an indication that a substantial flow of funds exists between planning districts, thus overstating the amount of capital being supplied in Districts III, IV, and V and understating capital supplied in the other districts.

If this discrepancy in the percentage of investment capital supplied by nonpersonal sources is caused by



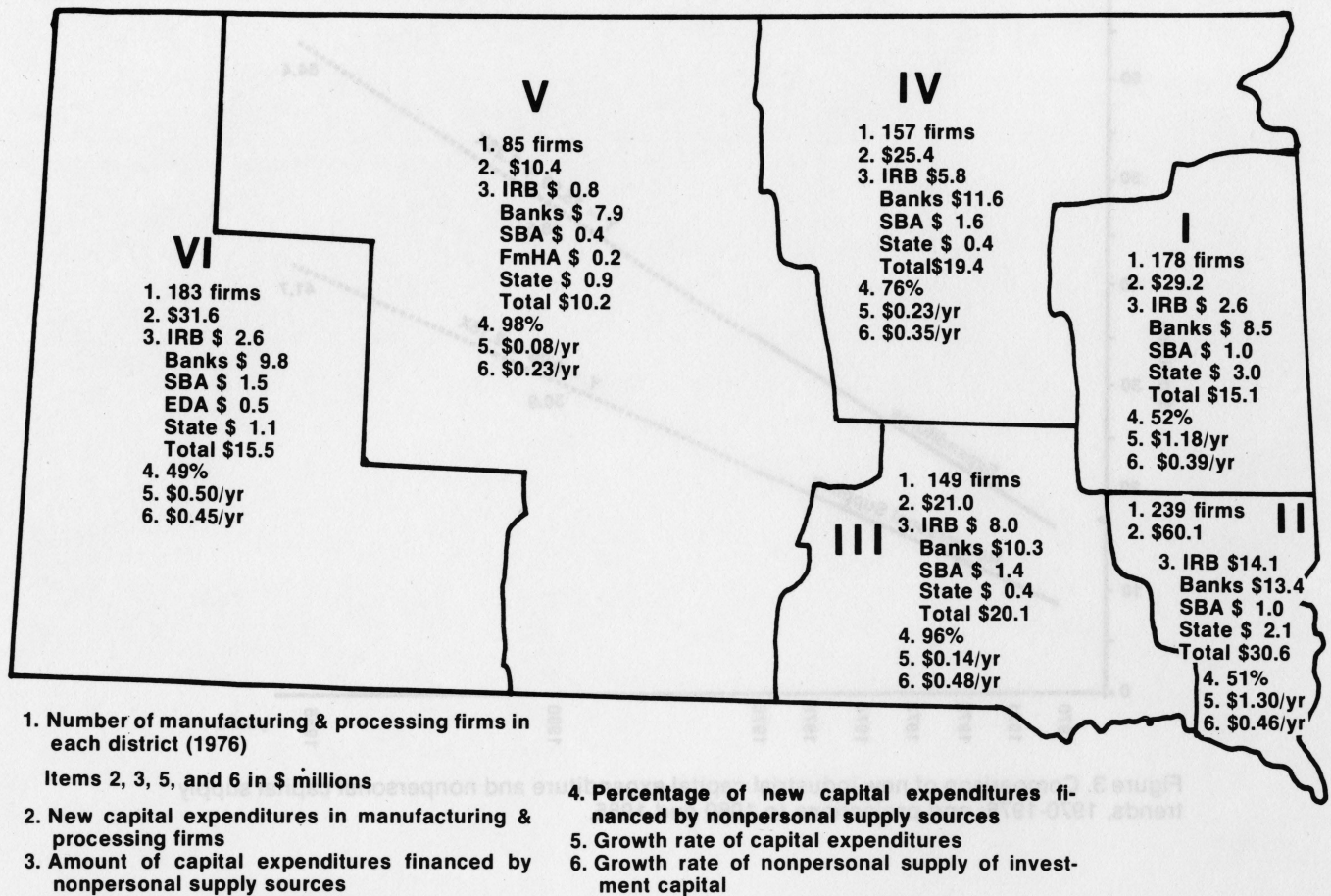


Figure 4. South Dakota industrial activity and financing by planning district, 1970-1976.

a flow of funds, the only source for which supply could be over- or understated would be the banks, since exact data were available for the other sources. Bank industrial loans could be over- or understated because of branch banking and correspondent banking. Since the data pertaining to commercial banks had to be estimated, it is also possible that the discrepancy may be explained as an error in estimate.

### State programs to encourage industrial development

The role of state government in industrial development can range from an all-out effort by the state to attract industry and (if need be) to finance it to a role of letting the state's economy take care of itself. The latter role appears to have vanished when one looks at the number of devices that state governments employ to attract industry.

The variety of programs indicates that there can be a great amount of competition among states when it comes to achieving industrial development. Common methods that states use to attract industry can be classified in three categories: direct financial assistance for industry, tax incentives, and special services for industrial development.

### Direct financial assistance

When states become involved in supplying direct financial assistance for industrial development, it could be suspected that the supply of investment capital from private sources is regarded as inadequate to meet the demand for capital, and that the state is trying to increase supply. It is also possible that the motive is to assist industrial development to move at a faster pace.

Programs that some states employ include state development authorities, state revenue or general obligation bond financing, state loans, state loan guarantees, or authorization enabling cities and counties to use such programs. A list of such activities used in South Dakota and in neighboring states is given in Table 3.

Because of similar economies, populations, natural resources, locations, and methods of transportation, South Dakota's most likely competition for new industry is from Montana, North Dakota, and Wyoming.

In comparison to these states, South Dakota's involvement in financing industrial development is quite limited. Of the programs listed in Table 3, only industrial revenue bond financing at the city and county level and a limited amount of direct industrial financing (by the Office of School and Public Lands) are currently authorized in South Dakota. A



Table 3. Alternative methods of financing industrial development by using state and local funds.

	Area states using method				Total number of states using method
	South Dakota	Montana	North Dakota	Wyoming	
State sponsored industrial development authority			*		31
State authority or agency revenue bond financing					17
State authority or agency general obligation bond financing			*		8
City and/or county revenue bond financing	*	*	*	*	43
City and/or county general obligation bond financing			*		20
State loans for building construction	*		*		14
State loans for equipment, machinery	*		*		11
City and/or county loans for building construction			*		8
City and/or county loans for equipment, machinery			*		8
State loan guarantees for building construction			*		11
State loan guarantees for equipment, machinery					9
State financing aid for existing plant expansions			*1		25
State matching funds for city and/or county industrial financing programs					5
State incentive for establishing industrial plants in areas of high unemployment			*		12
City and/or county incentive for establishing industrial plants in areas of high unemployment					7

Source: *Industrial Development*, Conway Research, Inc., Atlanta, Georgia, November/December 1974 issue. (Detailed information for all the states is included in the original article.)

<sup>1</sup>Permitted for electric generation and transmission facilities.

program of state loans and loan guarantees on a larger scale has been considered by the state legislature but has failed to win approval.<sup>15</sup>

Perhaps the reason this type of legislation has not passed is because of the memorable experience with the South Dakota Rural Credit Act of 1918 where the state made direct loans to farmers, only to have many of these loans default.

Montana and Wyoming authorize the use of industrial revenue bonds at the city and county level. They also authorize privately sponsored development credit corporations. Neither Montana nor Wyoming has specific programs which would use state funds for industrial development purposes.

North Dakota is more involved in the financing of industrial development than South Dakota, Montana, Wyoming, or for that matter most states in the country. Along with authorizing the use of most of the methods listed in Table 3, North Dakota has also established a state bank to be the depository of all

state funds along with funds from various other political subdivisions (7). The state bank cannot make private or commercial loans, but it can participate with other banks' commercial loans. North Dakota's state bank may also direct funds to industrial development by making loans to local development corporations in participation with the SBA.

Although there are many methods of financing industrial development available to state governments, availability of local financing does not appear to be of major importance to most firms. According to Tauer's survey of South Dakota industries, local financing rated seventh out of 10 factors which influence where a firm locates (11, p. 32). Factors such as home community of owner, closeness to markets, abundant labor, quality of life, closeness to raw materials, and a favorable tax policy had more influence on where a firm located than did availability of local funds.

### Tax incentives

Another method of attracting industry to a state is to offer a tax exemption or a tax moratorium.

Tax relief can be made on an individual basis and can be allowed on most state and local taxes. Possibilities include exemptions or moratoriums at the state or local level on taxes such as corporate income taxes, personal income taxes, excise taxes, property taxes, and sales and use taxes. These exemptions reduce the amount of revenues the state or local government would have received, but it is reasoned that the exemptions pay off in the long run and that lost revenues can be made up by increased revenues which occur due to spinoffs of new industries.

Communities hope that new industry may increase revenues by increasing employment, increasing income as firms compete for labor, and by creating a broader property tax base. Whether new industry results in positive or negative impacts on the net revenues of local governments is an unanswered question. Research on this question suggests that the impacts must be examined on a community by community basis (8).

South Dakota officials apparently have thought that the tax exemptions are very important in attracting industry to the state, as indicated by the variety of tax exemptions South Dakota offers (Table 4).

South Dakota offers a tax exemption on all state taxes except sales and use taxes.<sup>16</sup> It also allows local governments to exempt new firms from paying property taxes, although a payment in lieu of taxes may be made. Montana, North Dakota, and Wyoming also offer tax exemptions, although not as many types as South Dakota. Montana offers tax exemptions on land, capital improvements, and equipment for those industries which are based on natural resources. Wyoming is similar to South Dakota in that it also has no corporate or personal income tax. Wyoming also offers a tax exemption on inventories in transit, manufacturer's inventories, and on raw materials used in manufacturing. North Dakota offers tax exemptions on corporate income taxes, excise taxes, real property tax on equipment, inventories in transit, manufacturer's inventories, and on raw materials used in manufacturing.

### Special services

Special services which states and local communities may offer industries are additional

<sup>15</sup>Senate Bill No. 205, Forty-ninth Session Legislative Assembly, 1974, State of South Dakota, introduced by Senator Wollman, Representative Hersrud, and others, and Senate Bill No. 220, Fiftieth Session Legislative Assembly, 1975, State of South Dakota, introduced by Senator Krull and others.

<sup>16</sup>Although listed as tax exemptions, South Dakota has no personal income tax and the corporate tax is a bank franchise tax in reality.



Table 4. Tax incentives and other legal means used to entice industry to a state.

	Area states using method				Total number of states using method
	South Dakota	North Dakota	Wyoming	Montana	
Corporate income tax exemption	*1	*	*1		19
Personal income tax exemption	*1		*1		19
Excise tax exemption	*	*	*		10
Tax exemption or moratorium on land, capital improvements	*	*2			19
Tax exemption or moratorium on equipment, machinery	*	*2	*3		25
Inventory tax exemption on goods in transit (freeport)	*	*	*3	*	38
Tax exemption on manufacturer's inventories	*		*3	*	32
Sales/use tax exemption on new equipment				*4	31
Tax exemption on raw material used in manufacturing	*	*	*		43
Tax credits for use of specified state products					2
Tax stabilization agreements for specified industries					4
Tax exemption to encourage research and development					7
Accelerated depreciation of industrial equipment					20
State right to work law	*	*	*		19
Statewide uniform property tax evaluation law	*	*	*	*	40

Source: *Industrial Development*, Conway Research, Inc., Atlanta, Georgia, November/December 1974 issue. (Detailed information for all the states is included in the original article.)

\*South Dakota and Wyoming do not tax corporate or personal income.

\*\*For natural resource based industry only.

\*Personal property is not taxed in North Dakota.

\*Montana has no sales/use taxes.

methods of inducing industries to locate in their respective areas (Table 5).

Although special services do not involve making funds available to industries, they may involve use of state or city funds to provide services. Included in the special services could be financing for speculative building, provision of free or low cost land, state or municipally owned industrial parks, access roads, and other public works projects. City and county master plans, recreational projects, and various technical and manpower training services are also services which could assist in maintaining a sufficient labor force and a content management group.

As shown in Table 5, South Dakota supplied most of these special services except for those that call for direct state financing of speculative buildings, state provision of free land, or state owned industrial parks. North Dakota offers almost the same type of services as South Dakota. Montana and Wyoming are more restrictive about the types of services they offer, and are more inclined to make technical and manpower training services available than they are to have state funds directly used to promote industrial development.

#### Effect of inducements on industrial development

As shown in Tables 3, 4, and 5, states can become as involved with industrial development as they think necessary. States such as Montana and Wyoming appear to be taking the attitude that they should not become agencies for promoting industrial development. North Dakota, on the other hand, appar-

Table 5. Special services provided by state and local governments to entice industry to a state.

	Area states using method				Total number of states using method
	South Dakota	North Dakota	Wyoming	Montana	
State financed speculative building					4
City and/or county financed speculative building	*	*			17
Cities and/or counties provide free land for industry	*	*			13
State owned industrial park sites					7
City and/or county owned industrial park sites	*	*	*	*	48
State funds for city and/or county development related public works projects	*				28
State funds for city and/or county master plans	*				27
State funds for city and/or county recreational projects	*	*	*		33
State funds for private recreational projects					8
State program to promote research and development		*	*		34
State program to increase export of products	*	*	*	*	46
University R&S facilities available to industry	*	*	*	*	48
State and/or universities conduct feasibility studies to attract or assist new industry	*	*	*	*	49
State recruiting, screening of industrial employees	*	*	*	*	50
State supported training of industrial employees	*	*	*	*	50
State re-training of industrial employees	*	*	*	*	48
State supported training of "hard core" unemployed	*		*		33
State incentive to industry to train "hard-core" unemployed					20
State help in bidding on federal procurement contracts	*	*	*		27
State science and/or technology advisory council	*	*	*	*	45

Source: *Industrial Development*, Conway Research, Inc., Atlanta, Georgia, November/December 1974 issue. (Detailed information for all the states is included in the original article.)

ently has the attitude that it should provide financial assistance as well as tax incentives and special services if industrial development is going to occur. South Dakota's attitude appears to be one which the state will do all it can to attract industries except risk state funds for direct financing of firms. This does not preclude using School and Public Lands Funds as long as they are 100% guaranteed by the federal government.

Does it really make much difference which inducement techniques a state uses to encourage industrial development? According to information in Table 6 it does not appear to.

Tables 3, 4, and 5 indicate that Montana and Wyoming are less involved with industrial development at the state level when compared to neighboring states. But as Table 6 indicates, they have had growth in manufacturing employment, new capital expenditures, per capita personal in-



Table 6. Comparison of income and manufacturing employment growth in South Dakota and neighboring states, 1970-1975.

	South Dakota	North Dakota	Montana	Wyoming	
	(in 1,000's)				
<b>Employment in manufacturing</b>	1970	16	10	24	7
	1971	16	10	24	7
	1972	18	11	25	8
	1973	20	12	25	8
	1974	21	14	25	8
	1975	20	16	22	8
% Increase 1970-1975	25%	60%	-8%	14%	
	(\$ millions)				
<b>Capital expenditures for new plants &amp; equipment*</b>	1970	\$12.3	\$10.0	\$42.3	\$ 4.7
	1971	13.5	11.3	50.4	6.3
	1972	20.0	13.0	75.0	23.0
	1973	32.0	24.0	66.0	16.0
% Increase 1970-1973	160%	140%	56%	240%	
	(\$)				
<b>Per capita personal income</b>	1970	\$3165	\$2990	\$3370	\$3535
	1971	3446	3383	3479	3753
	1972	3716	3718	3897	4345
	1973	4771	5730	4626	4696
	1974	4281	5547	4776	5156
	1975	4980	5855	5434	5942
% Increase 1970-1975	57%	96%	61%	58%	
	(\$ billions)				
<b>Private non-farm personal income*</b>	1970	\$1.17	\$1.10	\$1.47	\$0.79
	1971	1.25	1.19	1.58	.88
	1972	1.30	1.20	1.70	.96
	1973	1.12	1.11	1.51	.88
% Increase 1970-1973	-4%	1%	3%	11%	

\*Figures for 1974 and 1975 are not available.

Source: U.S. Department of Commerce, Bureau of the Census, *Statistical Abstract*, Issues 1971-1976 (Washington: Government Printing Office).

come, and private non-farm income that is comparable to the growth of these categories in North Dakota and South Dakota where more active inducement policies have been used. North Dakota and South Dakota lead the other states in the volatile category of growth in manufacturing employment. They also have had substantial increases in annual rates of capital expenditures in manufacturing. However, Wyoming leads in this latter category—with the rapid growth in this category probably explained by coal development in both Wyoming and North Dakota.

The lack of clear differentials in the growth rates listed in Table 6 suggests that state financing of development projects, tax incentives, and special inducement services had little effect on industrial development in South Dakota and neighboring states. Of course, not shown is what would have happened to industrial development in these states had inducements not been used.

A hypothesis that might be derived from the data presented in Table 6 is that location, natural resources, and manpower advantages are more important than inducement techniques. This hypothesis is supported by the survey by Tauer (11, p. 32) of all manufacturing and processing firms in South Dakota. Tauer's survey indicated that favorable tax policies and availability of local funds rated seventh and eighth on a list of 10 factors influencing where a firm locates, with home community of owner, closeness to markets, abundant labor, and closeness to raw materials being the top four. Neither the data in Table 6 nor Tauer's survey is evidence that in-

ducements are not valuable to states desiring increased industrial development. Also unanswered is whether the benefits of inducements exceed their costs. Further research is needed on the effectiveness of inducements and on the net financial and other impacts of industry that might be attracted.

## Summary and conclusions

Industrial development in South Dakota requires annual increments of fixed and working capital. The question naturally arises whether sufficient funds will become available from internal and external sources to sustain an adequate rate of industrial growth.

Objectives of this study were to identify and describe nonpersonal sources of investment capital and to compare the projected availability of investment capital to anticipated need. The procedure followed was primarily descriptive.

New capital expenditures by manufacturing and processing firms were used as a proxy for effective demand for investment capital. From 1970 through 1976 those expenditures amounted to \$180 million. The 7-year trend of new capital expenditures indicates that those expenditures have been increasing at a rate of \$3.23 million per year. Keeping in mind the limitations of linear projections (which assume that future trends will mirror the past) these figures indicate that new capital expenditures could amount to an annual rate of about \$48 million by 1980 or \$64 million by 1985.

Table 7 illustrates the amount of financial assistance each potential nonpersonal source of supply for investment capital has furnished in recent years and the projected amounts which would be supplied if current trends continue. From Table 7 one can see that commercial banks and industrial revenue bonds have been the largest sources of investment capital and may well continue to be so.

A comparison of the amounts of new capital investments with the amount of investment capital supplied by nonpersonal sources reveals that at present there is apparently no capital shortage for industrial development in South Dakota.

Between 1970 and 1976 the nonpersonal sources which were studied supplied an average of 61% of the funds needed for new capital expenditures, leaving about \$10 million annually to be furnished by personal and corporate sources. Projections of industrial capital expenditures and nonpersonal supplies on the basis of the 1970-1976 trends indicate that by 1985 external-to-the-firm sources would supply 65% of industrial capital needs.

Should industrial capital shortages occur in South Dakota, methods of assistance used in other states

Table 7. Summary of the amount of investment capital supplied by nonpersonal sources.

	Capital supplied 1970-1976	1970-1976 growth rate	Project annual supply 1980	1985
	(\$ millions)			
Commercial banks	\$61.1	\$1.47	\$19.0	\$26.4
Industrial revenue bonds	33.5	0.32	7.0	8.6
SBA direct loans	7.2	-0.06	0.58	0.37
School & Public Lands Fund	7.9	0.56	5.48	8.26
EDA*	0.5	—	—	—
FHA**	0.2	—	—	—

\* Funds were made available only in 1970.

\*\*Industrial loans were made only in 1974.

Source: Table 2.



might be applied. Such methods include state loan and loan guarantees, state revenue or general obligation bond financing, and a state bank. In addition to state financing, tax incentives and special services can be employed to induce industrial expansion in the state.

As a result of the findings of this study, it is believed that a sufficient amount of investment capital is generated in South Dakota to finance a sustainable rate of industrial development. This conclusion was drawn not merely because estimated demand equalled the amount of funds already forthcoming, but also because of indications by lenders that more capital is available than is demanded.

The increasing percentage of funds for new capital expenditures being supplied by nonpersonal supply sources is also an indication of adequate investment capital being available for good industrial investment opportunities. Based on recent trends, the potential amount of capital available through personal and corporate sources added to the potential amount available from nonpersonal sources would be more than adequate for projected growth.

Banks will continue to be a major source of fixed capital for smaller new firms and for expanding firms. Industrial revenue bonds can supply much of the financing needed by large new firms. Other nonpersonal sources will continue to be useful but not major sources of investment capital.

The adoption of state programs to finance industrial development depends on legislative perception of the adequacy of present sources. State financing of industrial development does not seem necessary at present.

However, if state programs were adopted, they would add to the pool of funds available for industrial development and might stimulate faster industrial growth, particularly if they were made available to firms not eligible for financing from existing sources.

Natural resources and the availability of suitable labor appear to influence industrial development to a greater extent than state financing, tax incentives, or special services.

The adoption of a state loan guarantee program has been suggested in South Dakota, but as long as federal guarantee programs continue to be sufficiently funded, a state guarantee does not seem necessary. Investment of School and Public Lands Funds in industrial development projects has not met with serious public objection and, with funds available for expansion, may well meet the needs for state financing for industry for some time to come.

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