

498
POONA 4. SOIN
498

FORCES INFLUENCING INVESTMENT IN BUSINESS ENTERPRISE AFTER THE TRANSITION PERIOD

CHARLES CORTEZ ABBOTT

GOVERNMENT INSTITUTE OF POLITICS
POONA



X6529.73.N4
H4
046173

X6529.73.N4
H4
046173

DIVISION OF RESEARCH
SCHOOL OF BUSINESS ADMINISTRATION
HARVARD UNIVERSITY
CAMBRIDGE, BOSTON 63, MASSACHUSETTS

50 CENTS

FORCES INFLUENCING INVESTMENT IN BUSINESS ENTERPRISE AFTER THE TRANSITION PERIOD

The continuance of a high level of employment after the war is the publicly expressed desire of many businessmen. What are the financial problems which must be met if that desire is to become a reality? Data from which such a question can be answered by individual businessmen for their own companies are presented in "Forces Influencing Investment in Business Enterprise after the Transition Period." This is the fourth in a series of reports on current and postwar finances written by Charles Cortez Abbott, Associate Professor of Business Economics at the Harvard Business School. (April, 1944)

The following statement is a brief digest of the report.

The author estimates that, if a satisfactory level of employment is to be achieved, something like 17% more jobs need to be furnished than in 1940. Such a level of employment probably requires a gross national product of \$150 billion, compared with \$93 billion in 1929 and about \$88 billion in 1937 and 1939.

Will the condition of the fixed assets and the quantity of the current assets at the end of the war be adequate to produce this volume of output? The great bulk of the tremendous expansion in manufacturing facilities has taken place in a relatively few industries, and only a small portion of this new plant and equipment will be convertible to peacetime use. The majority of manufacturing concerns will emerge from the war period with their fixed assets inadequate for this purpose. There will be need of rehabilitation, expansion, and relocation.

Not only will funds for investment in fixed assets be required by business, but also additional working capital. In 1943 the government directly or indirectly supplied nearly half the assets used by industry for working capital purposes.

Two significant implications of this need for funds are: (1) A considerable portion of the financing should be in the form of equity financing or ownership. (2) Ownership therefore must be made more attractive than it has been recently.

Will the funds needed by business be available? Some of the forces influencing investment after the transition period will have sprung from prewar developments. Even before the war equity capital was not readily available, particularly for the moderate-size manufacturers in need of a relatively small amount of equity funds. Furthermore, the number of persons to whom business management could look to perform the function of ownership was declining, not only proportionately but perhaps also absolutely. These trends may continue into the postwar period.

The greatest single change in the supply of capital during the prewar period was the rise of "institutional savings" as shown by the increase in the assets of life insurance companies, investment trusts, savings banks, and pensions and retirement funds. Businessmen who must raise capital will look with interest on the tremendous amounts of funds annually becoming available for investment by these institutions.

The increasingly great emphasis placed on depreciation in business practice was another outstanding development in the 20 years ending in 1943. The new importance attached to depreciation, entailing as it does new psychological attitudes and new considerations in the making of business decisions, will continue to have far-reaching social and economic consequences. Two further changes of far-reaching significance for businessmen are the tremendous decline both in the volume of commercial loans since World War I and in the loans on securities of commercial banks since 1930.

Some of the forces influencing investment will come also from developments in the general field of government: (1) the Federal regulation of securities, (2) the continuation of government lend-

ing agencies, (3) the need of the Treasury, in view of the tremendous postwar debt, to maintain low and stable interest rates, (4) the "fiscal policy," i.e., the suggestion that the Federal Government fit into a coordinated and consistent policy the whole range of its activities that influence investment and expenditures by consumers.

Furthermore, there will be many legacies from the war. Just what all of them will be is hard to forecast. But certainly taxation belongs at the top of the list. Although after the war the country will have to pay heavier taxes, measured in terms of dollars, Professor Abbott holds out the possibility that the burden can be less onerous than the present or perhaps even the prewar load. But in order to bring this about, businessmen must make every effort to see that the postwar national income remains close to present levels, and framers of public policy must devise a postwar tax structure that will stimulate enterprise and must administer it in such a way as to impose on the taxpayer a minimum of hardship in compliance.

The accumulation of liquid funds in the hands of individuals may prove to be the single most important legacy of the war in the field of finance. From the point of view of society, it would appear most desirable that these new accumulations of capital should be invested in business enterprise, particularly in the form of equity.

Professor Abbott stresses the importance of motives, especially the distaste of individuals for the risks and responsibilities of ownership and the tremendous desire on the part of business managers to be free of debt. The effect of these two conflicting attitudes is a bar to investment expansion and hence militates against the provision of jobs.

The report closes with a statement of the necessity that ownership be made more attractive:

This matter, it seems clear, is one which is of vital and of equal importance to business management, to financiers, to labor,

and to framers of public policy. Ownership is the heart of the investment problem. It is the center of the employment problem. It is the basis on which credit is extended. It is the foundation on which the whole scheme of things in the American economy rests. If ownership is unattractive to potential investors, if owners are weak and irresponsible, if ownership as a function falls into disrepute, if directors and executives of business concerns fail to fulfill their responsibilities to owners, credit inevitably contracts, investment expenditure automatically declines, and unemployment necessarily develops.

(Division of Research, Harvard Business School, Soldiers Field, Boston 63, Massachusetts, 50 cents)

**FORCES INFLUENCING INVESTMENT IN
BUSINESS ENTERPRISE AFTER
THE TRANSITION PERIOD**

CHARLES CORTEZ ABBOTT

Associate Professor of Business Economics



DIVISION OF RESEARCH

**GRADUATE SCHOOL OF BUSINESS ADMINISTRATION
HARVARD UNIVERSITY**

SOLDIERS FIELD, BOSTON 68, MASSACHUSETTS

HARVARD UNIVERSITY
GRADUATE SCHOOL OF BUSINESS ADMINISTRATION
GEORGE F. BAKER FOUNDATION
DONALD K. DAVID, *Dean*
MELVIN T. COPELAND, *Director of Research*

Copyright, 1944

BY THE PRESIDENT AND FELLOWS OF HARVARD COLLEGE

PREFACE

This study, "Forces Influencing Investment in Business Enterprise after the Transition Period," is the fourth of a series of special reports dealing with the financial problems of business during the war and immediate postwar periods. The purpose of this series is to show the character of the financial problems which business concerns may face during the transition from war to peace, to develop the background against which these problems will appear, and to deal with a number of specific topics such as V and VT Loans.

The first report published in the series was "The Financial Situation of Industry after Two Years of War," by Charles Cortez Abbott (December, 1943); the second was "The V and VT Loan Arrangement and Termination Financing," by Charles Cortez Abbott and Walter G. O'Neil (January, 1944); and the third was "Business Finances during the Critical Transition from War to Peace," by Charles Cortez Abbott (February, 1944).

The author wishes to acknowledge the many helpful suggestions made by his colleagues, particularly those made by Professor Melvin T. Copeland, Director of Research of the Harvard Business School. The author is also grateful for the aid of Mr. Walter G. O'Neil who acted as his research assistant while this study was being prepared. The opinions in this report are the author's own, and errors and deficiencies are his responsibility.

CHARLES CORTEZ ABBOTT

Associate Professor of Business Economics

Soldiers Field
Boston, Massachusetts
April, 1944

INTRODUCTION	1
ASSETS OF BUSINESS AFTER THE WAR	4
Ownership	5
PURPOSE AND FRAME OF REFERENCE	6
Purpose	6
Prewar and Wartime Developments	7
Accounting Techniques: Statistical Measurements:	
Savings and Investment	7
Motives	9
Summary	10
LEGACIES OF THE 1920'S AND 1930'S	10
Supply of Capital and Credit	10
Stock Ownership	13
Reduction in Debt	14
Financial Attitudes and Practices	15
Commercial Banks	17
Government Activities and Fiscal Policy	18
Summary	20
LEGACIES OF THE WAR	20
Taxation	20
Liquid, Investable Capital	22
Dislocation of the Economy	23
New Types of Financial Institutions and Investment Policies	24
Summary	26
ACCOUNTING TECHNIQUES: STATISTICAL MEASUREMENTS:	
SAVINGS AND INVESTMENT	26
Expenditure by Business Firms for Investment Purposes	26
Investment in Business Enterprise	28
Investment Expenditure and Investment in Business Enterprise: Conclusions	30
Statistical Measurements	32
Statistical Measurements: Conclusions	37
Savings and Investment	38
"Oversaving" and Business Recession	39
Commentary	40
MOTIVES	42
General	43
Ownership	45
Financial Self-Sufficiency	46
Short-Term Interest Rates	47
Long-Term Interest Rates	48
Conclusion	49
SUMMARY	50