



Published on *Business, Political, and Cultural News in Fort Smith and Northwest Arkansas* (<http://www.thecitywire.com>)

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## The confidence factor

Submitted by The City Wire Staff on Thu, 01/17/2013 - 6:26pm

**Editor's note:** *Kathy Deck, the author of this commentary, is the director of the University of Arkansas at Fayetteville Walton College Center for Business and Economic Research. Her op-ed first appeared in the latest magazine issue of Talk Business Arkansas, which may be accessed at [this link](#) [1].*

Confidence is a funny thing.

The mere existence of confidence about the future among the players in an economy can lead to growth, while the absence of assurance often guarantees a slowdown. The situation is further complicated by the fact that there are different types of confidence:

- Consumers spend when their job prospects are good and their assets are rising in value;
- Businesses invest in new equipment and new workers when they expect demand for their products or services to grow; and,
- Citizens thrive when they believe that their political institutions will allow their concerns to be addressed.

A breakdown in any of these will cause uncertainty and caution, which leads to lowered growth prospects.

There are many economists who make careers out of studying decision-making in uncertain conditions. And, the condition of the Arkansas economy as we enter 2013 is one with a great deal of uncertainty about how long the confidence that has come from the economic recovery can be sustained.

To review the statistics, the Arkansas economy peaked with 1,214,200 jobs in December 2007. At the bottom of the job market in January 2010, the Arkansas economy had lost 80,100 jobs. As of late 2012, 44,300 of those jobs had been created again.

This still leaves a sizable hole from the pre-recession peak. Moreover, the sector effects have not been evenly distributed. Manufacturing, trade, and construction employment remain far below earlier levels, while health, education, and hospitality employment are at or near record levels. Where each industry goes from here is largely dependent upon the confidence of somebody (or a lot of somebodies).

The mood of “the Consumer” is abundantly important to the Arkansas economy. That is, both domestic and international buyers of consumer-packaged goods (the things you find at Walmart) determine the health of some of our key sectors, such as trade, transportation and utilities and manufacturing, which together comprise one-third of all jobs in Arkansas.

After falling to unprecedented low levels, American consumer sentiment has regained heights last seen in 2006.

Declining unemployment and rising prices for both homes and stock portfolios mean that household wealth is up. Unsurprisingly, total retail sales and outstanding consumer credit in the United States are at all-time record levels. However, for the consumer to continue buying, income levels have to show real growth. This is true at the international level as well, which is why Arkansas businesses pay such close attention to the state of the Euro zone and GDP growth in China.

Business confidence, of course, resides in the people who run those businesses. To even consider starting a company, an entrepreneur has to believe that there are customers, willing to pay good money for the product. Expanding an existing business by buying new equipment or hiring new employees also requires a leap of faith that the clients and buyers will keep coming.

The National Federation of Independent Businesses measures business optimism and has found a distinct lack of it among small businesses during the post-recession era. The top three reasons for the pessimistic outlook given by small business owners were lack of sales, taxes, and government regulations and red tape.

Another measure of business confidence comes from the Institute for Supply Management’s Report on Business. Medium-term prospects for both the manufacturing and service sectors are estimated by examining new orders, production, inventories, prices, etc.

The indexes indicate that early 2013 will be characterized by modest growth, with some risk factors including fuel price increases and regulatory uncertainty. The leaders of small and large businesses in Arkansas face the same macroeconomic environment and must optimize their organizations for a slow growth, risk-filled, globalized near-term horizon.

Regulatory and tax policy uncertainty are the kinds of things that the democratic process should be able to address. Voters elect representatives to implement the kinds of policies that lead to widespread prosperity. Confidence in the system of governance in the United States is crucial for ordinary people (who happen to be both consumers and business leaders) to make spending, savings, and investment decisions even in the face of usual economic uncertainty.

The beginning of 2013 should see noticeable declines in governmentally induced uncertainty. Both shorter and longer term federal tax and healthcare policies will be in place, which even if not to the preference of consumers and businesses, will provide the set of rules to the game.

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The political leaders of Arkansas should also continue to provide a sturdy state budgetary situation to keep confidence high at a more local level.

There is no doubt that the events which led to the recession in 2008 and the long, slow economic recovery since, have provided real challenges to optimistic outlooks. The decisions made by Arkansas consumers and businesses continue to be more cautious and well-thought out than before the crash.

These very rational responses to extreme events will continue to make the climb towards full recovery steep, but I'm confident that the climate of 2013 will be characterized by continued progress on the road to full employment, profitability, and economic prosperity.

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