

Small Business and State Growth: An Econometric Investigation

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For several years, the U.S. Census Bureau has produced firm-size data for the Office of Advocacy through its Statistics of U.S. Business (SUSB); see www.sba.gov/advo/research/data.html. With data spanning 1988 to more recent years, researchers willing to investigate linkages between small firm establishment births and deaths by state now have a sufficient number of observations to conduct their analysis.

The authors of this study utilize SUSB data to examine the effects of small firm establishment births and deaths on state-level changes in gross state product (GSP), state personal income (SPI), and total state employment for the years of 1988 to 2002.

Overall Findings

Small firm establishment births have a larger impact than any other factor examined on GSP, SPI, and total state employment. In fact, the authors find that small firm establishment birth rates and death rates have equal and opposite effects on state economic growth. This is a key finding, as it suggests that economic growth will be faster when the net small firm establishment birth rate is positive (i.e., when the birth rate exceeds the death rate).

The authors conclude that this general finding reveals that state efforts to promote small business formation will be more fruitful in terms of generating economic growth than virtually any other policy option in our models.

Highlights

- The authors find that increasing small business births by 5 percent would result in a 0.465 percent increase in GSP growth.
- The number of small firm establishments and the dollar value of small business payroll in neighboring states both have positive but small effects on own-state GSP growth.
- States with lower manufacturing shares of their GSP and states with a smaller share of their population between the ages of 45 and 64 (relative to the reference percentage of below age 25) have higher GSP growth.
- Faster state employment growth is associated with more large-firm activity, lower population density, fewer highly educated residents, a younger population, and a lower share of GSP from manufacturing. States without state-level inheritance, estate, or gift taxes also tend to have higher rates of employment growth. Similar trends emerge when analyzing changes in state personal income.
- The authors reached the same conclusions whether they defined a “small business” as less than 500 employees or as less than 100 employees.

Scope and Methodology

In this analysis, the authors explore the intricate relationships between small business activities and economic activity at the U.S. state level, using a panel of state data spanning the years 1988 to 2002. They examine a wide variety of indicators of state small business activity, including such things as simple counts of small business firms, establishments, employment, payroll, and the

number of small firm establishment births and deaths. Small business data are drawn from the U.S. Census Bureau's SUSB program, created from the annual County Business Patterns files with cooperation and partial funding from the Office of Advocacy.

To isolate the impact of small business activities on state economies, the authors control for other determinants of economic growth. The intent is to identify available policy instruments for state governments while controlling for as many possible determinants of economic growth as possible. A listing of data variables and sources can be found in Appendix Table 1 of the study.

This report was peer-reviewed consistent with Advocacy's data quality guidelines. More information on this process can be obtained by contacting the director of economic research at advocacy@sba.gov or at (202) 205-6533.

Ordering Information

The full text of this report and summaries of other studies performed under contract with the U.S. Small Business Administration's Office of Advocacy are available on the Internet at www.sba.gov/advo/research. Copies are available for purchase from:

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