

Looking Ahead: Opportunities and Challenges for Entrepreneurship and Small Business Owners

A working paper by

**Chad Moutray
Office of Advocacy
U.S. Small Business Administration**

for



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Looking Ahead: Opportunities and Challenges for Entrepreneurship and Small Business Owners

An Office of Advocacy Working Paper
by Chad Moutray [19] pages.

This paper was prepared for presentation at “Entrepreneurship in a Global Economy,” a conference sponsored by the Western New England College’s Law and Business Center for Advancing Entrepreneurship, held in Springfield, Massachusetts, on October 17, 2008.

Purpose

This paper outlines the most important issues and opportunities facing small business owners and entrepreneurs in this election year. While it does not delve into policy solutions, the next administration will almost certainly need to address many of them, regardless of who wins the presidency.

Challenges

The paper outlines five major challenges that small business owners will face in the coming years.

- **Strengthening the Overall Economy.** Small businesses continue to struggle in the economic downturn, and it will be important for policy leaders to get the economy moving again. Small businesses will be a large part of that, as entrepreneurs will spur new innovation and employment in the coming years. These firms will continue to be the job-generators that we have become accustomed to. With that said, industries will recover from the downturn in different ways, and some industries have clearly been hit harder this time than in past business cycles.
- **Taxes and Regulation.** Business conditions have a fundamental impact on entrepreneurial activity, and small business owners frequently cite tax and regulatory policies as a concern. Moving forward, it

will be important for policymakers to consider the impact of taxes and regulations on small business owners and would-be entrepreneurs.

- **Cost and Availability of Health Insurance.** Health insurance premiums have risen substantially in this decade. The Kaiser Family Foundation reports that the cost of employee-sponsored health insurance plans has increased 119 percent since 1999. It is also well-documented that employees at smaller firms are less likely to be offered health care coverage. Finding ways to control the cost of providing health insurance to employees and increasing coverage will remain a priority for our national and state leaders.

- **Attracting and Retaining a Quality Workforce.** Small businesses must compete for labor with their larger counterparts. This is more difficult in light of the disparity in total compensation, especially benefits, and the result is greater employee turnover. Demographic trends in the coming years might also exacerbate these challenges.

- **Global Competition.** American businesses face competitors on a number of fronts, both at home and abroad. The U.S. government has worked to increase the ability of our firms to compete overseas by lowering trade barriers. There are also some structural disadvantages that work to make our products less competitive, and many companies have reduced their costs by outsourcing some processes and tasks abroad. While insourcing also exists, many of these issues—especially the assertion that firms are “outsourcing jobs”—remains controversial; yet, firms argue that these are necessary strategies for survival in a global marketplace.

Opportunities

The paper also discusses five opportunities that small businesses will hopefully pursue in the next decade.

- **Increased Investments in Technology and Innovation.** There are strong linkages between innovation and new firm formation, and policymakers fully understand that risk-taking entrepreneurs have positive impacts on regional economic development. With many regional officials seeking the “next big thing” that will drive their local and regional economies for years to come, there is an appreciation that small businesses are leading the way toward new inventions, processes, and products. Such innovations are vital to our economic growth, and they will provide the tools to make our economy more competitive in an increasingly globalized marketplace.

- **“Economic Gardening” and Grooming Local Entrepreneurs.** Proponents of “economic gardening,” which has communities plow the dollars that would have been spent on luring big businesses to their town to promote local small businesses instead, argue that grooming existing firms can ultimately lead to greater payoffs in terms of job creation.

- **Pursuing New Markets Overseas.** One of the strengths in our current economic climate is the export sector, and international trade represents an opportunity for small businesses. Historically, many small business owners have not been proactive about trading with foreign partners. While 28.9 percent of the known export value stemmed from small firms, entrepreneurs have yet to fully tap the potential for growth in the export arena.

- **Promoting Business Ownership among Selected Demographic Groups.** Women and minorities have been extremely entrepreneurial over the past few years—a trend that is expected to continue. One of the driving factors for minorities has been the influx of immigrants coming to this country. Recent studies show a strong connection between immigration and high-technology entrepreneurship, suggesting enormous benefits for embracing these new citizens. In addition, many of the veterans returning home from Iraq and Afghanistan, are likely to devote themselves to entrepreneurship, as previous generations of veterans have done. Policymakers should find ways to promote greater business ownership among each of these groups.

- **Advancing Education and Training.**

Education and training are important as there are strong linkages between entrepreneurship and human capital. Moreover, small business owners devote significant resources to training their workforce. These firms are able to increase their labor productivity and reduce their labor turnover. In this way, small business owners should look at education not just as a means of retraining their workers, but also as methods of building new skills, developing new human talent, and preserving employee morale. Failure to do so might result in a reduced competitive position for the most talented employees.

Research Note

This report was peer reviewed consistent with the Office of 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 (202) 205-6533.

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LOOKING AHEAD: OPPORTUNITIES & CHALLENGES FOR ENTREPRENEURSHIP AND SMALL BUSINESS OWNERS

A Working Paper by Chad Moutray¹

Elections force us to evaluate where we are and where we would like to be in the future. In a few weeks, Americans will elect their next president. Voters will decide who can best lead the country at this important time in our history. Small business owners should also use this event to assess the impact of proposed policies on various opportunities and challenges facing their businesses.

Many of these opportunities and challenges for small businesses will be significantly affected by election proposals, and the two candidates often have expressed divergent policy views. This paper outlines five issues and five opportunities facing small business owners and entrepreneurs in this election year. I will leave specific policy solutions to others. They will almost certainly be addressed in the next administration.

Small businesses play a key role in the U.S. economy. There are many reasons why small firms matter in terms of policy and for our economic health. Small businesses—particularly newer ones in the first two years of operation—provide much of the net new job growth in our economy.² Between 2004 and 2005, nearly 83 percent of all of the net new jobs in our economy stemmed from businesses with fewer than 20 employees, according to the U.S. Census Bureau.³ Moreover, “high-impact firms” account for almost all of the private sector employment and revenue growth in the U.S. economy.⁴ As such, it is clear that new ventures are having a major impact on new employment, and it is for this reason that policymakers and economic development officials look toward entrepreneurship as an engine for future economic growth, especially in light of the current economic situation.

¹ The author is the chief economist and director of research for the Office of Advocacy of the U.S. Small Business Administration (SBA). This paper was presented at the conference “Entrepreneurship in a Global Economy,” sponsored by the Western New England College’s Law and Business Center for Advancing Entrepreneurship, in Springfield, Massachusetts, on October 17, 2008. The opinions expressed in this article are those of the author and do not necessarily reflect the views of the Office of Advocacy, the SBA, or the U.S. government. Thanks to Joseph Johnson, LaVita LeGrys, Jules Lichtenstein, and Radwan Saade for their helpful comments. Any errors or omissions can be attributed, however, to the author.

² Acs and Armington (2003).

³ The Office of Advocacy of the U.S. Small Business Administration partially funds the static and dynamic firm size data series from the Statistics of U.S. Business. These data typically have a three-year lag, with the most recent being from 2005. See http://www.sba.gov/advo/research/dyn_b_d8905.pdf.

⁴ “High-impact firms” are enterprises that have experienced a doubling of sales and employment over a four-year period. See Acs, Parsons, and Tracy (2008).

CHALLENGES

This section outlines five major challenges that small business owners will face in the coming years. These are (1) strengthening the overall economy, (2) taxes and regulation, (3) the cost and availability of health insurance, (4) attracting and retaining a quality workforce, and (5) global competition.

Strengthening the Overall Economy

The most obvious challenge facing small business owners right now is the economy. While an official recession has not been declared by the National Bureau of Economic Research, the U.S. economy has been weak and is expected to remain so after the election. Real gross domestic product grew by an annualized 2.8 percent in the second quarter of 2008, mostly due to a sharp increase in exports and increased consumer spending because of economic stimulus checks. Yet, this growth has been one bright spot in an otherwise downbeat economic situation in 2008. As of this writing, we have lost 760,000 nonfarm payroll jobs since December 2007, with losses in each month so far this year, and the unemployment rate has risen to 6.1 percent.⁵ Behind the scenes, a series of factors have contributed to extreme levels of individual and small business anxiety, such as rising oil prices, sharp declines in the housing sector, and a weakened financial position of banks and other financial institutions.

For their part, small business owners have struggled, along with their larger counterparts, to weather the economic downturn. The National Federation of Independent Business (NFIB) continues to show that owners are less willing than in previous years to expand their small businesses, to hire additional workers, to invest in new plant and equipment, or to borrow money. In a shift from recent years, their top concern is now inflation (it had been the high cost of health insurance for the past few years).⁶ Small businesses have taken a wait-and-see approach to the challenging economic environment, with most postponing the exploration of any new opportunities at least until there are signs that the economy is improving. In the meantime, many firms are looking for ways to streamline their operations or to re-evaluate their business model, paying closer attention to their balance sheet.⁷

⁵ These numbers reflect September 2008 employment numbers, which were released on October 3, 2008.

⁶ See *Small Business Economic Trends* from the National Federation of Independent Business, which is published monthly and is available at <http://www.nfib.com/page/sbet>. In addition, the Federal Reserve Board publishes a quarterly report, *Senior Loan Officer Opinion Survey on Bank Lending Practices*, which recently has shown tougher lending standards and reduced demand for small firm commercial and industrial loans. This report is available at <http://www.federalreserve.gov/boarddocs/SnLoanSurvey/>.

⁷ These comments came from a webinar on small businesses and weathering the economy. It was sponsored by SAP and myventurepad.com on September 25, 2008. In addition, various users of LinkedIn.com provided their own advice

For small business owners, significantly higher energy costs affect both the bottom line and the demand for their products and services. In 2001, the average cost of a barrel of crude oil was \$25.92; by 2007, that figure had grown to \$72.37. By July 2008, crude oil prices had swelled to over \$145 a barrel. Today, many would agree that the oil price bubble has burst, with oil prices fluctuating between \$90 and \$120 per barrel.⁸ While lower oil prices are helpful, small businesses must get used to energy costs that are drastically higher than in past years. Moreover, small businesses, especially in manufacturing and commercial sectors, face greater energy price differentials than their larger competitors due to economies of scale, putting them at a disadvantage.⁹

Moving forward, it is important to get the economy moving again. Small businesses will be a large part of that, as entrepreneurs will spur new innovation and employment in the coming years. These small firms will continue to be the job-generators that we have become accustomed to. With that said, industries will recover from the downturn in different ways.¹⁰ Construction and financial services, due to the bursting of the housing bubble, have clearly been hit harder this time than in past business cycles. Construction, in particular, is overwhelmingly dominated by small businesses—over 86 percent of firms in this sector are considered small. This sector has lost 558,000 jobs since January 2007. Only one other major industrial sector lost more jobs in that same time period—manufacturing, with a loss of 587,000 jobs.

Taxes and Regulation

Business conditions affect entrepreneurial activity, and small business owners frequently cite tax and regulatory policies as a concern. Research has shown that marginal tax rates influence firm formation and exit¹¹ and state-level policies that promote business creation lead to higher employment, gross state product, and personal incomes.¹² Along these lines, we know that small businesses face disproportionately higher compliance costs per employee than their larger counterparts when complying with federal regulations,¹³ and the federal government and a majority of states have aggressively pushed regulatory flexibility protections for small businesses when drafting new rules.¹⁴ Other nations, as well, are pushing to reduce business regulatory

on this issue in conjunction with the forum; see http://www.linkedin.com/answers/startups-small-businesses/small-business/STR_SMB/328271-5714444?goback=.srp_1_1222238801916_in.

⁸ This range reflects the highly volatile closing price of West Texas crude oil from August and September 2008.

⁹ Bollman (2008).

¹⁰ Joel Popkin and Company (2003).

¹¹ Bruce and Gurley (2005) and Gurley-Calvez (2005).

¹² Bruce et al. (2007).

¹³ Crain (2005).

¹⁴ U.S. Small Business Administration (2008).

barriers, as documented each year by the World Bank, and overall business activities in these countries have likely increased as a result.¹⁵

With these facts in mind, a number of tax and regulatory changes will take place in the coming years, and small business owners will be paying close attention to each of these. At the federal level, several tax provisions of 2001 and 2003 are set to expire after FY 2010, and there will be a lot of debate over which ones will be extended and which should be allowed to expire. Government leaders will also need to address the alternative minimum tax at some point, which continues to affect more and more small businesses each year, and state governments continue to grapple with fiscal pressures that affect their tax policies.¹⁶ On the regulatory front, it is anticipated that there will be a significant influx of new regulations at the federal level on issues ranging from homeland security to finance. As these rule changes are considered, small business interests will need to be thoroughly considered.

Cost and Availability of Health Insurance

Health insurance premiums have risen substantially in this decade. The Kaiser Family Foundation reports that the cost of employee-sponsored health insurance plans has increased 119 percent since 1999, with a 5 percent increase in 2008 from the previous year.¹⁷ These premium increases have forced small business owners to make changes to the coverage they offer their workers, including sharing the cost of coverage with their employees, pursuing lower cost options such as consumer-driven plans, or choosing not to offer health coverage at all. A recent survey by the NFIB found that nearly half of all small business owners shopped around for health care coverage in the past three years; however, only 1 to 2 percent dropped coverage altogether. The report goes on to suggest, “The reason for stagnation or decline in the number of small businesses offering health insurance, therefore, appears to be that the owners of new firms are increasingly reluctant to offer it.”¹⁸

It is well-documented that there are 46 million Americans who do not have health insurance,¹⁹ and many of those people work for a small business. Indeed, research continually shows that employees at smaller firms are less likely to receive health insurance or other benefits than those at larger firms.²⁰ While virtually all of the employers with 200 or more employees offered health benefits to their workers, only 62 percent of business with fewer than 200

¹⁵ World Bank Group (2008).

¹⁶ Bruce (Forthcoming, 2008).

¹⁷ Kaiser Family Foundation and the Health Research & Educational Trust (2008).

¹⁸ National Federation of Independent Business (2007).

¹⁹ DeNavas-Walt, Proctor, and Smith (2008).

²⁰ Joel Popkin and Company (2005) and Econometrica, Inc. (2007).

employees offered such benefits in 2008. For very small firms with 3 to 9 employees, the offer rate was 49 percent.²¹ Part of the challenge is that it costs more to administer small health plans than it does larger ones.²² There have been several legislative proposals that would have allowed small business to “pool” together to reduce such costs. None of these bills have passed Congress, however.²³

The cost and availability of health insurance has long been a concern for small business owners, and prior to the current economic situation, it was their top concern on the monthly NFIB survey for several years. Finding ways to control the cost of providing health insurance to employees and increasing coverage will remain a priority, as well, and policymakers will almost certainly grapple with these issues over the next few years.

Attracting and Retaining a Quality Workforce

Small businesses must compete effectively for labor with their larger counterparts. This is more difficult in light of the disparity in total compensation, especially benefits, and the result is greater employee turnover. Research shows that firms that offer benefits have a 26.2 percent lower probability of having an employee leave in a given year; moreover, the provision of benefits increases the probability of the employee staying another year by 13.9 percent.²⁴ Firm size is a major determinant in whether a business offers such benefits.

Demographic trends in the coming years might exacerbate the challenges for small businesses in terms of employee recruitment and retention. There are 78.2 million Americans who are part of the Baby Boomer generation born between 1946 and 1964,²⁵ and the first wave of this group has already begun to retire, a process that will accelerate over the next decade. These retirements pose two problems for businesses, both large and small. First, firms will see a mass exodus of “institutional knowledge” that will be hard to replace in certain fields. For that reason, many businesses have contemplated ways to entice more of these retirees to delay their departure, if possible, but more likely, it poses a challenge for these firms to effectively train others to step into these roles once the retirees leave. Second, the exit of Baby Boomers could lead to labor shortages in some industries, particularly in technology and health occupations. Labor shortages suggest that firms may engage in bidding wars for skilled workers, and small businesses are

²¹ Kaiser Family Foundation and the Health Research & Educational Trust (2008)

²² Chu and Trapnell (2003).

²³ The most recent example of this is the bipartisan Small Business Health Options Program (SHOP) Act (S. 2795), which promotes the “pooling” of health insurance plans for employers with fewer than 100 employees and for the self-employed.

²⁴ Hope and Mackin (2007).

²⁵ U.S. Department of Commerce, Bureau of the Census (2006).

sometimes at a competitive disadvantage in these. When these positions go unfilled, small businesses are forced to seek other alternatives, such as having existing employees work more hours, leaving positions vacant, or turning down work.²⁶

Businesses, of course, have also explored hiring talented foreign workers, especially in math, science, and engineering. The U.S. benefits from having a skilled workforce whether those employees were native or foreign born. There is a lot of evidence that immigrants are extremely entrepreneurial, with one study stating that 25 percent of the new engineering and technology companies were started by immigrants.²⁷ With this in mind, policymakers need to find ways to encourage the legal immigration of these high-skilled employees, which is currently very difficult to do for both small and large firms.²⁸

Global Competition

As Thomas Friedman, notes, the world is growing “flatter” and Americans face competitors on a number of fronts, both at home and abroad.²⁹ Much has been written on this topic, as the debate over globalization continues to garner attention in academic, media, and political circles. The U.S. government has worked to increase the ability of Americans to compete overseas by lowering trade barriers.³⁰ Government can also help ensure that trade laws are enforced.

Recently, the National Association of Manufacturers (NAM) released studies on the structural costs of lowering manufacturing costs in the United States compared with its trading partners. They found that U.S. manufacturers pay 31.7 percent more in nonproduction costs relative to the nation’s nine largest trading partners. Much of the difference is accounted for in higher costs for tax and regulatory compliance, energy expenditures, health and retirement benefits, and tort litigation.³¹ U.S. businesses can effectively compete if they continue to meet the needs of their customers, rely on cutting-edge technology and innovation, and keep their businesses flexible and entrepreneurial (including exploring new markets through exporting).³²

One way American companies have been able to reduce their costs is by outsourcing some processes and tasks abroad. By producing some inputs elsewhere at a lower cost, firms can more effectively compete on price while focusing domestic production efforts in other areas. To

²⁶ National Federation of Independent Business (2001).

²⁷ Wadhwa et al. (2007).

²⁸ Schramm and Litan (2008).

²⁹ Friedman (2005).

³⁰ For more information on small business opportunities and exports, see Moutray and Tobias (Forthcoming, 2008).

³¹ Leonard (2003, 2006).

³² RSM McGladrey (2006).

the extent that this practice may be seen as “outsourcing jobs,” it is controversial and not without real costs. But arguments can be made on both sides: foreign companies often outsource work to the United States as well—a practice known as “insourcing”—and proponents of offshoring—the relocation of business processes from one country to another—suggest that it is a necessary strategy for firm survival in a global marketplace.³³

OPPORTUNITIES

This section outlines five opportunities that small businesses will hopefully pursue in the next decade. These are (1) increasing investments in technology and innovation, (2) grooming local entrepreneurs for growth (“economic gardening”), (3) pursuing new markets overseas, (4) promoting entrepreneurship among women, minorities, veterans, and immigrants, and (5) advancing education and training.

Increased Investments in Technology and Innovation

Many economic development officials are seeking the “next big thing” that will drive local and regional economies for years to come. Research shows that universities that invest heavily in research and development tend to inspire new firm formations in the areas that surround them,³⁴ and governments now regularly promote technology transfer as an important component of economic development.³⁵ Furthermore, regions with greater entrepreneurial growth have been associated with higher levels of innovation and technology use,³⁶ and states that promote new firm formation through public policy are more likely to experience higher employment, incomes, and overall output.³⁷ Therefore, policymakers of both political parties understand that risk-taking entrepreneurs have a positive impact on regional economic development.³⁸

These entrepreneurial ventures, especially the university spin-offs, depend on new inventions. One way to track the propensity to invent is through patent filings. A new study being released by the U.S. Small Business Administration’s Office of Advocacy shows that 40 percent of the companies that issued at least 15 patents over a five-year period were small businesses. In

³³ StratEdge (Forthcoming, 2008).

³⁴ Kirchoff and Armington (2002).

³⁵ Shane (2004).

³⁶ Camp (2005).

³⁷ Bruce et al. (2007).

³⁸ See Moutray (2007) for a summary of the Office of Advocacy’s research linking entrepreneurship with regional economic development.

addition, these small firms produced significantly more patents per employee than the larger firms in the sample.³⁹ This and other studies show that small businesses are more likely to develop emerging technologies than their larger counterparts. The authors of the new study observe that “Small firms are more likely to attempt to build a business around a new emerging technology, whereas in general it appears large firms work on emerging technologies in order to improve an existing product line or business.”⁴⁰ This paper goes on to identify emerging industries that favor small businesses; these include: imaging and display, nanotechnology, photonics and optical components, and biomedical and biotechnology pipeline firms. Thus, small firms are actively engaged in the cutting-edge technologies that will shape our future growth. These findings are not new, as they have been documented before in earlier Office of Advocacy research.⁴¹ But it is encouraging to note that they are consistent with past results. A previous study from this office, for instance, found that industries that heavily employ scientists and engineers are “more accommodating to small fast-growing private firms”; whereas, larger production-focused industries tend to have more large firms.⁴²

Innovation and entrepreneurship have provided a strong foundation for economic growth in the United States, and the Office of Advocacy has been committed to studying this relationship. In fact, one of the first reports that this office released was a 1979 report from a task force on small business and innovation. Among its conclusions, it stated that:

“Innovation is an essential ingredient for creating jobs, controlling inflation, and for economic and social growth. Small businesses make a disproportionately large contribution to innovation. There is something fundamental about this unusual ability of small firms to innovate that must be preserved for the sake of healthy economic and social growth.”⁴³

Nearly thirty years later those words are still true. Innovations are still vital to our economic growth, and they will provide the tools to make our economy more competitive in an increasingly globalized marketplace. Moreover, it is the risk-taking entrepreneur who will often champion these innovations, helping to drive our American economy forward.

“Economic Gardening” and Grooming Local Entrepreneurs

Policymakers eager to show that they are bringing jobs to their district or their state have two options: “economic hunting” versus “economic gardening.” The first strategy involves

³⁹ Breitzman et al. (Forthcoming, 2008), pp. 6-7.

⁴⁰ *Ibid.*, p. 30.

⁴¹ CHI Research, Inc. (2003) and Baumol (2005).

⁴² Eckhardt and Shane (2006).

⁴³ U.S. Small Business Administration (1979).

offering generous incentives to lure large businesses. Success can bring a lot of publicity and ultimately a number of high-quality employment opportunities for the area. With that said, not everyone wins at the game of “chasing smokestacks.” Some regions will never be able to out-bid others for these high-profile acquisitions of firms and jobs. An alternative strategy seeks to groom existing small businesses for growth. Chris Gibbons—the director of business and industry affairs for the city of Littleton, Colorado, and a champion of “economic gardening”—argues that if communities were to plow the dollars spent on luring big businesses to their town to promote local small businesses instead, the payoff could be greater. Convincing policymakers to think long-term instead of in political cycles, though, can often be a hard sell.⁴⁴

Pursuing New Markets Overseas

American businesses have long sought opportunities where they could find them. For those able to sell their goods and services to new markets, international trade can provide an excellent opportunity. As mentioned earlier, one of the strengths in the economy right now is the export sector. Real exports increased an annualized 13.2 percent in the second quarter of 2008, and these figures have risen steadily, outpacing the growth in imports, since 2005. (Note that the U.S. still imports over \$380 billion more in goods and services that it exports; although, the trade deficit has recently improved somewhat.) International trade represents an opportunity for small businesses. Collectively, 239,287 small businesses are known to have been involved in the export business in 2006, the most recent year that data by firm size was reported by the U.S. Census Bureau. These companies constituted 97.3 percent of all known exporters, and they engaged in \$260 billion in known export transactions—28.9 percent of the total. While more-recent figures are not currently available, we can assume that small firms have continued participating at the same rate.

Overseas markets can provide new customers for small business owners, but entrepreneurs have yet to fully tap their potential for growth in the export arena. U.S. small businesses have often ignored the global marketplace. Demand for their products and services was sufficient in local markets, and there was no need to enter into the complexities of trading with foreign customers. Size has often been a challenge for many smaller firms, as small business owners could not afford to devote an employee’s time to pursuing foreign deals. Research, for instance, has shown that small businesses were generally not very proactive in exploring export markets. Businesses that did engage in international trade often did so based on

⁴⁴ Quello and Toft (2006).

inquiries instead of a strategic initiative, or by becoming subcontractors to larger firms who were engaged internationally.⁴⁵

Promoting Business Ownership among Selected Demographic Groups

Entrepreneurship has long been seen as a way to better one's self, and research has documented the role that business ownership can play in lifting an individual's overall standard of living.⁴⁶ While those pursuing self-employment are varied, studies show that those individuals who opt to become their own boss are more likely to be older white males with greater overall wealth.⁴⁷ Despite those findings, other demographic groups have been extremely entrepreneurial over the past few years—a trend that is expected to continue.

Women and minorities have seen large increases in business ownership in the past few decades. For instance, the number of women-owned employer firms increased 8.3 percent between 1997 and 2002 (the year of the most recent economic census), with women-owned firms totaling 6.5 million or 28.2 percent of the total.⁴⁸ Over the same time period, minority business ownership also soared, with African-Americans, Asians, and Hispanics seeing the largest gains. In 2002, minorities owned 18 percent of the total number of businesses, and Hispanic-owned firms constituted the largest portion with 6.6 percent of all U.S. firms.⁴⁹ One of the driving factors behind some of these numbers—particularly for Asians and Hispanics—has been the influx of immigrants coming to this country. As mentioned earlier, there is a strong connection between immigration and high-technology entrepreneurship,⁵⁰ suggesting that Americans should embrace the influx of new citizens to its shores; moreover, where differences do exist between native-born and immigrant self-employment rates, these can often be explained by financial, human capital, and legal barriers.⁵¹

Another group that will receive more attention in the coming years is the veterans' community, including those who were disabled in service. With the U.S. fighting wars in both Iraq and Afghanistan, many of these individuals will devote themselves to private enterprise upon completing their service to this country. If this new generation is anything like their predecessors, they will be highly entrepreneurial. Past research, for instance, shows that military service is a major determinant of self-employment, and veterans experience higher self-

⁴⁵ Palmetto Consulting (2004).

⁴⁶ Bates (1997) and Lowrey (2004).

⁴⁷ Moutray (2007).

⁴⁸ Lowrey (2006).

⁴⁹ Lowrey (2007).

⁵⁰ Wadwha et al. (2007).

⁵¹ Fairlie and Woodruff (2006).

employment rates than non-veterans.⁵² One study suggested that 22 percent of veterans in the population were purchasing or starting a new business or considering doing so.⁵³ In 2002, veteran-owned firms represented 14.5 percent of the total respondent business owners to the U.S. Census Bureau's Survey of Business Owners (or 12.2 percent of the respondent firms).⁵⁴ Policymakers should find ways to promote greater business ownership among veterans, women, and minorities in the coming years.

Advancing Education and Training

Increasing educational attainment is one way for us to improve our own potential, but greater human capital also has broader implications for our nation and our economy. For instance, many researchers have studied the linkages between education and economic development, and in general, they conclude that regions with more highly educated citizens tend to be more entrepreneurial and to experience more rapid economic growth.⁵⁵ Along those lines, regions with greater educational levels also tend to have reduced poverty.⁵⁶ Greater educational attainment means increased incomes and various opportunities. For the purposes of this paper, there are strong linkages between entrepreneurship and human capital. Indeed, there is evidence that baccalaureate education is a strong influence on the decision to become self-employed, and the various attributes of the college experience also play into the employment decision.⁵⁷

From the perspective of small businesses, it is important to keep in mind that small businesses are often the first employers of many Americans, and these workers are often less educated than the rest of the population. As a result, small businesses must devote significant resources to training their workforce.⁵⁸ Nonetheless, small firms that invest in training and development are able to increase their labor productivity, and they are also able to reduce labor turnover.⁵⁹ In this way, small business owners should look at education not just as a means of retraining their workers, but also as a method for building new skills, developing new human talent, and preserving employee morale. Here again, though, it is worth noting that small firms are less likely to offer benefits to their workers than their larger counterparts; therefore, a failure

⁵² Moutray (2007) and Fairlie (2004).

⁵³ Waldman Associates and REDA International (2004).

⁵⁴ Lichtenstein and Sobota (2007).

⁵⁵ Florida (2002); Georgellis and Wall (2000); Glaeser (1998); Lee, Florida, and Acs (2004); and others.

⁵⁶ Bates (1997) and Goetz (2007).

⁵⁷ Moutray (December 2007; Forthcoming, 2008) and Weaver, Dickson, and Solomon (2006).

⁵⁸ Lichtenstein (Forthcoming, 2008).

⁵⁹ Hope and Mackin (2007).

to invest in training and development could also result in a reduced competitive position for the most talented employees.

Finally, education can also be looked at as a means for promoting innovation. Universities, especially since passage of the Bayh-Dole Act of 1980, aggressively push “technology transfer” programs whereby academically-sponsored research leads to new commercialized ventures in the community.⁶⁰ This phenomenon—where innovation provides the linkages for greater entrepreneurship—was discussed earlier, but it is further proof that investments in education can pay off.

CONCLUSION

Small businesses are an integral part of the country’s social and economic fabric. Americans have long championed the essential role that so-called “mom-and-pop” stores play in promoting our society’s basic values and in our economy. Encouraging small business ownership and new firm creation, though, means more to our economic success than simply the preservation of Main Street values. Entrepreneurship injects vitality and a competitive spirit into our economic landscape that is not readily available from large business. Research shows that small firms play a vital role, for instance, in innovation, regional economic development, and the pursuit of new markets. These firms are responsible for half of our real gross domestic product, employ half of the private workforce, and generate the majority of our net new jobs. Moreover, self-employment serves as an opportunity for many of our citizens to better themselves by taking their fate (and risks) into their own hands and generating new businesses.

Small business owners, though, face enormous challenges in the coming years, and policymakers will need to wrestle with these issues after this year’s election. First and foremost, we need to revitalize our nation’s economy, which has struggled for much of this year. Americans are worried about the state of the economy, and in addition to greater economic volatility in general, small businesses must now contend with lower sales, higher input prices, and increased global competition. Reducing such anxieties and strengthening the economic picture will go a long way toward getting these firms back to what they do best—expanding their businesses, hiring new workers, and investing in new technologies to find their niche. Other long-term challenges are equally important to resolve. For instance, small businesses are eager for a business tax and regulatory environment that allows them to prosper without being overly burdensome, and they worry about maintaining and attracting a quality workforce. The fact that

⁶⁰ Shane (2004).

smaller businesses are less able to provide and retain the generous benefits of their larger counterparts makes the competition for talent that much harder.

In conclusion, the future for small business in the United States is very bright. Leadership from both political parties embrace policies that stimulate entrepreneurship and its contributions to our economy and to our competitive strength in the global marketplace. This paper has outlined some of the opportunities and challenges that await small business owners. Clearly, there are many others that I could have highlighted, as well. Americans will head to the polls in a matter of weeks. Many of us will be looking to our leaders for solutions to the challenges confronting small businesses across the country. Putting in place policies that promote economic growth and stability will allow entrepreneurs to more easily exploit the opportunities that confront them.

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