SBA Office of Advocacy
www.sba.gov/advo

Small Business Research Summary

Advocacy: the voice of small business in government

July 2007 No. 307

The Effect of Wealth and Race on Start-up Rates

By Maritza Salazar (BCT Partners, LLC), 2007. 35 pages
Newark, NJ 07103 under contract no SBAHQ-05-M-0416

Purpose

The notion that it "takes money to make money" is commonplace in public discourse. Indeed, some researchers find that the ability to start a business would be greatly impaired without some form of financial assets or net wealth. Others, however, have found that some businesses do not require large amounts of start-up capital, and therefore, one's financial position has little to do with whether or not an individual is able to start their business.

Understanding the role of wealth in predicting the likelihood of becoming self-employed may be particularly relevant for nascent minority entrepreneurs.

This research uses the Panel Study of Entrepreneurial Dynamics (PSED) to uncover whether wealth affects the start-up outcomes of minorities and nonminorities differently

Overall Findings

At first glance, net wealth is not found to be related to the likelihood that an entrepreneur will start a company. However, a more fine-grained analysis shows that net wealth is positively correlated with the probability that a nascent entrepreneur will start a new company if the nascent entrepreneur is in the top 25 percent of the wealth distribution. This research also shows that wealth affects the outcomes of minority entrepreneurs slightly differently than it influences the outcomes of their white counterparts.

Highlights

- The results show that Black and Hispanic nascent entrepreneurs face greater odds in opening a business than do their nonminority counterparts. Race is a significant predictor of opening a business, and the odds of a minority person opening a business are found to be 55 percent lower than those for a nonminority.
- Female nascent entrepreneurs in the sample were also less likely to start a business than males.
- Having a parent who was or is an entrepreneur has no influence on the likelihood of opening a business.
- Those individuals who sought start-up dollars from financial institutions were more likely to operate their business successfully than those who did not seek financial assistance.
- Nascent entrepreneurs with no experience in the industry of their start-ups were less likely to open a business than those with experience.
- Other factors for which the researcher tested hypotheses were also not as important in influencing the likelihood that a nascent entrepreneur will open a business. These include the existence of a business plan, locating in a "high technology state" (California, Massachusetts, or Texas, as defined by the author), the size of the nascent entrepreneur's household, the number of partners in the start-up, or the level of educational attainment.

Scope and Methodology

The authors analyzed the impact of wealth on business creation using a multi-year sample from the PSED where nascent entrepreneurs were interviewed in 1998, 1999, 2000, and 2001. Several decisions were made regarding truncating the data sample for the analysis. First, any respondent who reported that a firm would be sharing over 50 percent of the start-up was removed from the sample to ensure that the entrepreneurial activity of individuals (and not firms) is being assessed. In addition, based on other studies using the PSED dataset, only respondents between the ages of 25 and 45 were examined. Respondents not within this range were excluded from the sample, as very few were involved in entrepreneurial activity.

To study the relationship between the likelihood of opening a new business and underlying factors including race, net wealth, and other personal characteristics, the author estimated a logistic regression specification with the binary outcome of whether or not an entrepreneur opened a business at any point during the evaluated years 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 (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:

National Technical Information Service
5285 Port Royal Road
Springfield, VA 22161
(800) 553-6847 or (703)605-6000
TDD: (703) 487-4639
www.ntis.gov
Order number: PB2007-109051
Paper A04 ($29.50)
Microfiche A01 ($14.00)
CD-ROM A00 ($22.00)
Download A00 ($17.95)

To receive email notices of Advocacy's newsletter, press, regulatory news, and research, visit **http://web.sba.gov/list.** For really simpole syndication, visit **www.sba.gov/advo/rsslibrary.html**.