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Small Business Research Summary

Advocacy: the voice of small business in government

March 2010 No. 359

An Analysis of Small Business and Jobs

by Brian Headd, Office of Advocacy, 2010. [21] pages.

Purpose

Interest in understanding small businesses' role in the labor market has been heightened in the current economic climate because of small businesses' prodigious job generating ability. This report is a primer for understanding some basic facts and trends in small business employment, as well as an introduction to the data available to form opinions and develop hypotheses.

Overall Findings

Small and large firms have differing roles in the labor market, and their status as creator or destroyer of jobs varies throughout the business cycle. Business start-ups (almost all of which are small) are incredibly valuable to the labor market in the long term, continuing businesses provide most of the net new jobs, and business locations with large employment swings dominate net employment results and fluctuate most in response to the economy.

Highlights

Two kinds of data are used to characterize small firms' role in the labor market: static and dynamic data. Static data are used to illustrate the shares of jobs in small and large firms; these are essentially snapshots in time. Dynamic data track how firms got from point A to point B, and what happened to jobs along the way. For instance, the static view shows the amount of jobs in small firms while the dynamic view shows job growth, job decline, and net job change in small and large firms.

Static Results—Share of Employment

• About one half of the private-sector is employed by small businesses and the other half by large businesses. Or, put another way, 60 million people were employed by smalls, and 60 million by large (2006 data).

• The share of small firm employment underwent a slight decline during the late 1990s and leveled off in the 2000s. The share tends to decline when the economy is doing well and increases when the economy struggles; this reflects the tendency of firms to expand when the economy is expanding (and average firm size increases) and to shrink when the economy struggles.

• Small firms' employment share of the private sector (along with the economy's average firm size) is a reflection of economies of scale, which are largely affected by the economy as a whole, technology, consumer preferences, the fortunes of various industries, financing, and a myriad other factors.

• Small firms' share of part-time workers is similar to large firms' share: 21 percent and 18 percent, respectively, for 2008.

• Small firms tend to support underserved demographics, employing higher shares of Hispanics, individuals with lower educational attainment (high school degree or less), and individuals aged 65 or older.

Dynamic Results—Share of Net Job Creation

• Over the past 15 years, small businesses have accounted for the majority of private-sector net job creation. The two official data sources differ as to how great the small business share is. According to the Bureau of Labor Statistics, small businesses create about 65 percent of the net new jobs (Business Employment Dynamics figures); according the Bureau of the Census, they create about 90 percent (Statistics of U.S. Businesses).

- Business turnover is the domain of small businesses. Over the past few decades, about 95 percent of both new employer births and employer deaths took place in firms with fewer than 20 employees. This is not surprising as about 90 percent of employers have fewer than 20 employees.
- Identifying the key players in job creation depends on how you frame the analysis. One approach shows that small firm employment creation is greatest at start-up. For a cohort of firms tracked from birth, the number of jobs that the cohort creates is greater at birth than at any time in the following 20 years, as employment losses from firm deaths outweigh job gains resulting from expansions.
- Another official data source shows that existing firms play the predominant role in net job creation. Quarterly data show continuing establishments accounting for 69 percent of the net new jobs from 1993 to mid-2008. The remaining 31 percent are the net of jobs created in establishment births minus those lost in establishment deaths.
- The decline in job turnover over the past five years or so is a concern in that it represents a decline in "creative destruction," or the replacement of old firms by new ones in the course of economic and industrial progress.
- The bulk of employment change takes place in a small number of firms that have relatively large employment swings. From 1992 to mid-2009, establishments with employment changes of 20 or more employees (gains and losses) accounted for 57 percent of the net employment change.

Scope and Methodology

For research purposes, a small business is defined as a firm with fewer than 500 employees. Note that a firm is an aggregation of all establishments (or employer business locations) owned by a parent company.

The report presents facts, figures, and charts drawn mainly from the Bureau of Labor Statistics' Business Employment Dynamics (BED) and the U.S. Census Bureau's Statistics of U.S. Businesses (SUSB). BED is available quarterly on a six- to nine-month lag, while SUSB is available annually on a two- to three-year lag. SUSB has precise geographic and industry detail, while BED has limited detail. BED also classifies firms using dynamic sizing (responding to the regression to the mean issue) while SUSB uses start-year sizing.

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.

Ordering Information

The full text of this report is online at **www.sba.gov/advo/research/rs350tot.pdf.** The text and summaries of other working papers and 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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