

Small Business and Self-Employment as Income Mobility Mechanisms

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Small firm contributions to the labor market entry, skill training, and wage growth of youth were extensively documented in an earlier series of research studies, which confirmed that small businesses provide most first-time job opportunities for young labor market entrants. The skills and experience of those entry jobs paid off handsomely for the youth, as witnessed by their subsequent wage growth.

Using the National Longitudinal Surveys of Youth (NLSY), this study tracks employment and income experiences in a later phase of the typical work life. Whereas the earlier studies focused on the first years of labor market entry for youths aged 14-22 in 1979, this study focuses on those same workers a decade later. The author tracks the work history of young people who were 24-32 years at the beginning of the observation period (1989) over the subsequent 15 years. At the end of 2004, the respondents were aged 39-47.

The research goal was twofold. The first goal was to gauge the degree of relative income mobility over the 1989-2004 period by ascertaining how often and to what degree individuals changed intra-cohort income ranks in this period. The second goal was to isolate the role of small business exposure in the mobility process.

Overall Findings

The key overall finding was that relative income mobility continued to be the norm even as workers got older and more experienced, and it is a pervasive phenomenon in the U.S. labor market. The incidence and magnitude of income-rank change were no lower in the 1990s than in earlier decades. In other words, men who were moving up and down

their age-specific hierarchy in the 1980s were still changing rank-order positions in the 1990s. A key specific finding is that the incidence and extent of mobility are higher for self-employed individuals than for paid employees.

Highlights

Mobility

- Although earnings mobility is a pervasive phenomenon, the experience is not shared equally. As in earlier decades, workers at the top and bottom ranks of the earnings distribution are less likely (45-50 percent) to move than are workers in the middle of the distribution (75-82 percent).
- This differential mobility has increased slightly over time, thereby intensifying longer-term inequities.
- In contrast to the 1980s experiences, mobility among female workers (73.2 percent) was actually higher than among male workers (69.8 percent) in the 1990s.
- Female workers have also experienced much higher exit rates (75-85 percent) from the lowest ranks of the distribution than their male counterparts.
- Self-employed individuals are more mobile than paid employees. In other words, self-employed workers experience more year-to-year changes and volatility in income than payroll workers. Greater income volatility is a feature of self-employment.
- For males, self-employment and small business experience is associated with net downward mobility, particularly in relation to individuals with no such exposure. For women, the patterns are similar, with the single exception of women who are self-employed at the outset of the observation period; this situation is associated with upward mobility.

Factors affecting persons employed in or owning a small business:

- Whites are more likely to experience self-employment than minorities.
- Those who work in small establishments or self-employment have lower educational attainment than their counterparts in the full sample.
- Early marriage (before 1989) significantly reduced the incidence of self-employment or small establishment experience for men, but substantially increased the incidence of self-employment for women.
- There are no significant differences across employment subsamples in either age or work experience, except for women, where work experience is inversely correlated with small-establishment employment.

Scope and Methodology

The research uses the NLSY work history data. The overwhelming advantage of the NLSY is its longitudinal tracking of individual workers. By stringing together the responses in each survey, a 28-year work history of an individual can be constructed. From the universe of NLSY respondents, a core sample of 4,776 workers with significant work experience over the 15-year period 1989-2004 was identified. Significant employment was defined as individuals with at least \$3,800 of income. Other criteria for selecting the sample were that an individual had to be “attached,” i.e., employed in both 1989 and 2004—the end year of the observation period. Identifying an individual’s small business experience proved difficult because the NLSY did not ask questions about employer size every year, nor did it use the same questions every time. The most frequent focus was on establishment, rather than firm size. Even when firm size was asked, the results were severely aggregated so that only firms with under and over 1,000 workers could be identified. Therefore, the author designated a “small business” subsample of 1,955 workers in single-establishment small firms with fewer than 100 employees.

To determine whether a unique profile exists for persons employed in or owning a small business, the author compared the characteristics of individuals across five employment subsamples: 1) small, single-establishment firms (“small business”) in 1989, 2) self-employed in 1989, 3) never in a small establishment or self-employment (during the 1989-2004 period), 4) ever in a small establishment (during the 1989-2004 period), and 5) ever in self-employment (during the 1989-2004 period). The author attempt-

ed to identify statistically significant differences between the means in each of these five subsamples and the full “core” sample. The analysis was performed separately for men and women.

The purpose of isolating workers who are self-employed or employed in small businesses was to assess their differential mobility experiences. This was done by comparing the mobility experiences of the self-employed or those working in small businesses with the mobility experiences of the total core sample. The assessment of mobility was conducted in relative terms, i.e., the extent to which individuals change relative income position as a result of differential income growth. Income rank distributions for various years were identified. The hierarchy of incomes was partitioned into 20 equal-sized ranks (each equal to 5 percentage points) or “ventiles.” “Mobility” was defined as a move of at least two ventiles, i.e., a rank movement of at least 5 percentage points between 1989 and 2004. Three aspects of “mobility” were measured: 1) percent of workers changing ranks (percent mobile), 2) average total distance moved without regard to direction (mean absolute change), and 3) average net distance moved, based on direction (mean algebraic change).

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