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Small Business Research Summary

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The Nonemployer Start-up Puzzle

A working paper by Zoltan Acs, Brian Headd, and Hezekiah Agwara, 2009 [24] pages.
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Purpose

Nonemployer firms—businesses without employees—represent a large percentage of businesses; however, little is known about their dynamics (entry and exit). This report seeks to illustrate basic statistics about the prevalence of entry and exit for nonemployers and the local conditions that led to their entry.

Overall Findings

Nonemployer start-up rates across states and industries seems countercyclical to labor market changes, while employer start-up rates move in line with overall economic cycles. These characteristics of start-up rates indicate that starting a nonemployer firm is more likely to be an occupational decision, while employer firm start-ups are more likely to be responses to economic opportunity.

Highlights

- Nonemployer firms have entry rates about three times those of employer firms. Of the existing companies in 2004, 34.3 percent of nonemployers were new and 12.6 percent of employers were new.
- Exit rates were lower than but similar to entry rate levels for both nonemployers and employers.
- Entry and exit rates (collectively referred to as turnover) seem associated with an industry's economies of scale (essentially, amount of capital needed for entry). Mining, with its high economies of scale, had low turnover rates, while service industries, with low economies of scale, had high turnover rates.
- Employer birth and exit rates had a wider distribution by industry than those of nonemployers. This attribute is most likely because the sizes of employer firms have a wider range than nonemployers, which by definition are restricted in growth of payroll.
- Florida and Nevada had the highest combined birth and exit rates over the period of analysis, most likely the result of the states' tendencies toward service-type industries and their growing economies. States with warmer climates in general had higher turnover, with Georgia and Texas in the top five states for turnover. East Coast states leaned toward low turnover, with Pennsylvania and Connecticut in the five states with the lowest turnover.
- Average receipts size for nonemployer births by industry ranged widely. Educational services had by far the lowest receipts sizes; wholesale trade the highest.
- The econometric model found, after controlling for population growth, that the states' unemployment rates were positively correlated with nonemployer entry and were the main driver at the state level.
- The main driver for employer entry was state real GDP; unemployment also had a positive impact.

Scope and Methodology

The report uses special tabulations produced by the U.S. Census Bureau's Nonemployer Statistics and funded by the U.S. Small Business Administration, Office of Advocacy. Nonemployer firms are essentially businesses without payroll but with annual receipts above $1,000. For data years 2002-2004, Census matched nonemployers across years to determine entry and exit by major industry and state.

In addition to causal observations about the tabulations, the report uses econometric models to determine the factors associated with the entry of nonemployers, such as local economic conditions and an area's human capital. Employer entry from the U.S. Census Bureau's Statistics of U.S. Businesses program was also modeled for comparison purposes.

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/rs354tot.pdf.** Summaries and text 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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