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

CHAD MOUTRAY*

Elections, especially those where the incumbent is not running, force us to evaluate where we are and to look to the future for where we would like to be. 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 have a chance to do the same, as they can use this event to assess the impact of proposed policies on various opportunities and challenges facing their businesses.

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

Small businesses play a key role in the United States economy. There are many reasons why small firms matter in terms of policy and for our nation's 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.¹ Between 2004 and 2005, nearly eighty-three percent of all net new jobs in our economy stemmed from businesses with fewer than twenty employees.²

* Chief economist and director of research for the Office of Advocacy of the United States Small Business Administration (SBA). 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 United States 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.

1. Zoltan J. Acs & Catherine Armington, *Endogenous Growth and Entrepreneurial Activity in Cities* (Ctr. for Econ. Studies, U.S. Census Bureau, CES-WP-03-02, 2003).

2. OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., EMPLOYER FIRM BIRTHS AND DEATHS BY EMPLOYMENT SIZE OF FIRM, 1989-2005 (2005), http://www.sba.gov/advo/research/dyn_b_d8905.pdf. The Office of Advocacy of the SBA partially funds the

Moreover, “high-impact firms” account for almost all of the private sector employment and revenue growth in the United States economy.³ 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.

I. CHALLENGES

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

A. *Strengthening the Overall Economy*

One significant 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 economy in the United States has been weak and is expected to remain so after the election. Real gross domestic product grew by an annualized 2.8% in the second quarter of 2008, mostly due to a sharp increase in exports and increased consumer spending because of economic stimulus checks.⁴ Yet, this growth has been one bright spot in an otherwise downbeat economic situation in 2008. As of this writing,⁵ we have lost 1.4 million nonfarm payroll jobs since December 2007, with losses in each month so far this year, and the unemployment rate has risen to 6.2%.⁶ Behind the scenes, a series

static and dynamic firm size data series from the Statistics of United States Business. This data typically has a three-year lag, with the most recent being from 2005.

3. ZOLTAN J. ACS, WILLIAM PARSONS & SPENCER TRACY, U.S. SMALL BUS. ADMIN., *HIGH-IMPACT FIRMS: GAZELLES REVISITED 2* (2008), <http://www.sba.gov/advo/research/rs328tot.pdf>. “High-impact firms” are enterprises that have experienced a doubling of sales and employment over a four-year period. *Id.* at 17.

4. OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., *QUARTERLY INDICATORS—SECOND QUARTER 2008: THE ECONOMY AND SMALL BUSINESS 2* (2008), <http://www.sba.gov/advo/research/sbqei0802.pdf> [hereinafter *QUARTERLY INDICATORS—SECOND QUARTER 2008*]. Note that the figures in this Article reflect revisions made to the data since the release of this publication.

5. This Article was presented on October 17, 2008. Year-to-date figures would reflect known data points for the year up to that point; however, changes have been made to this Article to reflect data revisions made after-the-fact.

6. BUREAU OF LABOR STATISTICS, U.S. DEP’T OF LABOR, *THE EMPLOYMENT SITUATION: SEPTEMBER 2008*, at 3, http://www.bls.gov/news.release/archives/empisit_100320

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. Data provided by the National Federation of Independent Business (NFIB) shows that owners are less willing than in previous years to expand their small businesses, to hire additional workers, to invest in new plants and equipment, or to borrow money.⁷ Their top concern, which had been the high cost of health insurance for the past few years, is now inflation.⁸ Small businesses have taken a wait-and-see approach to the challenging economic environment, with few exploring new opportunities at least until there are signs of improvement. In the meantime, many of them are looking for ways to streamline their firms' operations or to re-evaluate their business models, paying closer attention to their balance sheets.⁹

For small business owners, significantly higher energy costs affect both the bottom line and the demand for their products and services. The average cost of crude oil in 2001 was \$25.92 per barrel; in 2007, that figure grew to \$72.37 and ended the year much higher than that.¹⁰ By July 2008, crude oil prices had swelled to

08.pdf. These numbers reflect September 2008 employment numbers, which were released on October 3, 2008. *Id.*

7. See generally WILLIAM C. DUNKELBERG & HOLLY WADE, NAT'L FED'N OF INDEP. BUS., NFIB SMALL BUSINESS ECONOMIC TRENDS (2009), http://www.nfib.com/object/IO_39981.html.

8. See WILLIAM C. DUNKELBERG & HOLLY WADE, NAT'L FED'N OF INDEP. BUS., NFIB SMALL BUSINESS ECONOMIC TRENDS 18 (2008), http://www.nfib.com/object/IO_38976.html. In addition, the Federal Reserve Board publishes a quarterly report, which recently has shown tougher lending standards and reduced demand on small firm commercial and industrial loans. See FED. RESERVE BD., THE OCTOBER 2008 SENIOR LOAN OFFICER OPINION SURVEY ON BANK LENDING PRACTICES (2008), <http://www.federalreserve.gov/boarddocs/SnLoanSurvey/200811/fullreport.pdf>.

9. These comments came from a September 2008 webinar sponsored by SAP, a business software company, and myventurepad.com, a business networking website, on small businesses and weathering the economy. See SAP United States, <http://www.sap.com/usa/about/index.epx> (last visited May 15, 2009); MyVenturePad, <http://myventurepad.com/> (last visited May 15, 2009). In addition, various users of LinkedIn provided their own advice on this issue in conjunction with the forum. See, e.g., What Measures Should Small Businesses Take to Weather this Economic Downturn?, http://www.linkedin.com/answers/startups-small-businesses/small-business/STR_SMB/328271-5714444?goback=.srp_1_1222238801916_in (last visited May 15, 2009).

10. OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., QUARTERLY INDICATORS—THIRD QUARTER 2008: THE ECONOMY AND SMALL BUSINESS 2 (2008), <http://www.sba.gov/advo/research/sbqei0803.pdf>.

over \$145 a barrel.¹¹ Today, many would agree that the oil price “bubble” has burst, with oil prices hovering between \$90 and \$120 per barrel.¹² 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, which puts them at a disadvantage.¹³

Going 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 to which we have become accustomed. That said, industries will recover from the downturn in different ways,¹⁴ and some industries, such as construction and financial services, due to the bursting of the housing bubble, have clearly been hit harder this time than in past business cycles.¹⁵ Construction, in particular, is overwhelmingly dominated by small businesses—over eighty-six percent of firms in this sector are considered small—and over 583,000 jobs have been lost since December 2006. The only other major industrial sector that lost more jobs in that same time period was manufacturing, with a loss of 713,000 jobs.¹⁶

B. *Taxes and Regulation*

Business conditions impact entrepreneurial activity, and small business owners frequently cite tax and regulatory policies as a concern. Research has shown that marginal tax rates impact firm formation and exit¹⁷ and that state-level policies that promote business creation lead to higher employment, gross state product, and per-

11. *Id.* at 1.

12. This range reflects the highly volatile closing price of West Texas crude oil from August and September 2008. *See id.*

13. ANDY BOLLMAN, U.S. SMALL BUS. ADMIN., CHARACTERIZATION AND ANALYSIS OF SMALL BUSINESS ENERGY COSTS 1 (2008), <http://www.sba.gov/advo/research/rs322tot.pdf>.

14. *See* JOEL POPKIN & CO., U.S. SMALL BUS. ADMIN., SMALL BUSINESS DURING THE BUSINESS CYCLE 48 (2003), <http://www.sba.gov/advo/research/rs231tot.pdf>.

15. OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., QUARTERLY INDICATORS—FOURTH QUARTER 2008: THE ECONOMY AND SMALL BUSINESS 1 (2008), <http://www.sba.gov/advo/research/sbqei0804.pdf>.

16. *Id.* at 2.

17. DONALD BRUCE & TAMI GURLEY, U.S. SMALL BUS. ADMIN., TAXES AND ENTREPRENEURIAL ACTIVITY: AN EMPIRICAL INVESTIGATION USING LONGITUDINAL TAX RETURN DATA 1 (2005), <http://www.sba.gov/advo/research/rs252tot.pdf>; TAMI

sonal incomes.¹⁸ Along these lines, small businesses face disproportionately higher compliance costs per employee than their larger counterparts when complying with federal regulations,¹⁹ and the federal government and a majority of states have aggressively pushed regulatory flexibility protections for small businesses when drafting new rules.²⁰ Other nations, as well, are pushing to reduce business regulatory barriers, as documented each year by the World Bank. Overall business activities in these countries have likely increased as a result.²¹

With these facts in mind, a number of tax and regulatory changes will take place in the coming years, and small business owners should be paying close attention to each of these. At the federal level, several tax provisions of 2001 and 2003 are set to expire after fiscal year 2010, and there will be much 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 affects more small businesses each year, and state governments continue to grapple with fiscal pressures that impact their tax policies.²² 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 contemplated, small business interests will need to be thoroughly considered.

C. *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% since

GURLEY-CALVEZ, U.S. SMALL BUS. ADMIN, HEALTH INSURANCE DEDUCTIBILITY AND ENTREPRENEURIAL SURVIVAL 1 (2005), <http://www.sba.gov/advo/research/rs273tot.pdf>.

18. DONALD BRUCE ET AL., U.S. SMALL BUS. ADMIN, SMALL BUSINESS AND STATE GROWTH: AN ECONOMETRIC INVESTIGATION 2 (2007), <http://www.sba.gov/advo/research/rs292tot.pdf>.

19. W. MARK CRAIN, U.S. SMALL BUS. ADMIN., THE IMPACT OF REGULATORY COSTS ON SMALL FIRMS 6 (2005), <http://www.sba.gov/advo/research/rs264tot.pdf>.

20. See OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., REPORT ON THE REGULATORY FLEXIBILITY ACT FY 2006, AT 45-46 (2007), <http://www.sba.gov/advo/laws/flex/06regflx.pdf>.

21. See WORLD BANK GROUP, DOING BUSINESS 2009 (2008), available at http://www.doingbusiness.org/Documents/FullReport/2009/DB_2009_English.pdf.

22. Donald Bruce, *A Tax Policy Update for America's Small Businesses*, in OFFICE OF ADVOCACY, U.S. SMALL BUS. ADMIN., THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 147 (2009), http://www.sba.gov/advo/research/sb_econ2008.pdf [hereinafter REPORT TO THE PRESIDENT 2008].

1999, with a 5% increase in 2008 from the previous year.²³ These premium increases have forced small business owners to make changes to the coverage that they offer their workers, including sharing the cost of such coverage with their employees, pursuing lower cost options such as consumer-driven plans, or choosing not to offer such 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 one to two percent dropped coverage altogether.²⁴ The survey suggests: “The reason for stagnation or decline in the number of small businesses offering employee health insurance, therefore, appears to be that the owners of new firms are increasingly reluctant to offer it.”²⁵

It is well-documented that there are almost forty-six million Americans who do not have health insurance, and many of those people work for small businesses.²⁶ Indeed, research continually shows that employees at smaller firms are less likely to receive health insurance or other benefits than those at larger firms.²⁷ While virtually all of the employers with two hundred or more employees offered health benefits to their workers, for instance, only sixty-two percent of businesses with less than two hundred employees offered such benefits in 2008. For very small firms with three to nine employees, the offer rate was forty-nine percent.²⁸ Part of the challenge is that it costs more to administer small health plans than it does larger ones,²⁹ and, as a result, there have been several legislative proposals that would have allowed small business to “pool”

23. KAISER FAMILY FOUND. & HEALTH RESEARCH & EDUC. TRUST, EMPLOYER HEALTH BENEFITS: 2008 ANNUAL SURVEY 1 (2008), <http://ehbs.kff.org/pdf/7790.pdf> [hereinafter EMPLOYER HEALTH BENEFITS].

24. NAT'L FED'N OF INDEP. BUS., NATIONAL SMALL BUSINESS POLL: PURCHASING HEALTH INSURANCE 1, 11 (2007), http://www.411sbfacts.com/files/purchasing_health.pdf.

25. *Id.* at 1.

26. CARMEN DENAVAS-WALT, BERNADETTE D. PROCTOR & JESSICA C. SMITH, U.S. CENSUS BUREAU, INCOME, POVERTY, AND HEALTH INSURANCE COVERAGE IN THE UNITED STATES: 2007, at 22 (2008), <http://www.census.gov/prod/2008pubs/p60-235.pdf>.

27. ECONOMETRICA, INC., U.S. SMALL BUS. ADMIN., STRUCTURAL FACTORS AFFECTING THE HEALTH INSURANCE COVERAGE OF WORKERS AT SMALL FIRMS 2 (2007), <http://www.sba.gov/advo/research/rs295tot.pdf>; JOEL POPKIN & Co., U.S. SMALL BUS. ADMIN., COST OF EMPLOYEE BENEFITS IN SMALL AND LARGE BUSINESSES 1 (2005), <http://www.sba.gov/advo/research/rs262tot.pdf>.

28. EMPLOYER HEALTH BENEFITS, *supra* note 23, at 4.

29. ACTUARIAL RESEARCH CORP., U.S. SMALL BUS. ADMIN., STUDY OF THE ADMINISTRATIVE COSTS AND ACTUARIAL VALUES OF SMALL HEALTH PLANS 1 (2003), <http://www.sba.gov/advo/research/rs224tot.pdf>.

together to reduce such costs. However, none of these bills has passed Congress.³⁰

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.³¹ 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 in the next few years.

D. *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% 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%.³² Firm size is a major determinant in whether a business offers such benefits.³³

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 1964,³⁴ 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 large and small businesses. 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 departures. More likely, the businesses will be challenged to effec-

30. The most recent example of this is the bipartisan Small Business Health Options Program (SHOP) Act, S. 2795, 110th Cong. (2008), which promotes the “pooling” of health insurance plans for employers with less than one hundred employees and for the self-employed.

31. See generally NAT’L FED’N INDEP. BUS., SMALL-BUSINESS OWNERS AND HEALTH CARE POLICY: NFIB HEALTH-CARE SURVEY—SUMMARY OF RESULTS (2007), <http://www.nfib.com/Portals/0/PDF/AllUsers/5.21.2007ExecSumNFIBHealthCare.pdf>.

32. JOHN B. HOPE & PATRICK C. MACKIN, U.S. SMALL BUS. ADMIN., THE RELATIONSHIP BETWEEN EMPLOYEE TURNOVER AND EMPLOYEE COMPENSATION IN SMALL BUSINESS 22 (2007), <http://www.sba.gov/advo/research/rs308tot.pdf>.

33. See *supra* notes 26-30 and accompanying text.

34. Press Release, U.S. Census Bureau, Facts for Features: Oldest Baby Boomers Turn 60! (Jan. 3, 2006), http://www.census.gov/Press-Release/www/releases/archives/facts_for_features_special_editions/006105.html.

tively train others to step into these roles once the retirees leave.³⁵ Second, the loss of “Baby Boomers” could lead to labor shortages in some industries, particularly in technological and health occupations.³⁶ Labor shortages suggest that firms might need to compete for skilled workers by outbidding one another, and small businesses are sometimes at a competitive disadvantage when doing so. When positions go unfilled, small businesses are forced to seek other alternatives, such as increasing the hours worked by existing employees, leaving positions vacant, or turning down work.³⁷

Businesses, of course, also explore hiring talented foreign workers, especially in the fields of math, science, and engineering. The United States benefits from having a skilled workforce comprised of both native and foreign-born employees. There is a lot of evidence that immigrants are extremely entrepreneurial, with one study stating that twenty-five percent of the new engineering and technology companies were started by immigrants.³⁸ With this in mind, policymakers need to find ways to encourage the legal immigration of these high-skilled employees.³⁹

E. *Global Competition*

As Friedman notes, the world is growing “flatter” and Americans face competitors on a number of fronts, both at home and abroad.⁴⁰ Much has been written on this topic, as the debate over globalization continues to garner attention in academic, media, and political circles. The United States government has worked to increase the ability of Americans to compete overseas by lowering

35. See, e.g., Joe Mullich, *They Don't Retire Them They Hire Them*, WORKFORCE MGMT., Dec. 2003, at 49.

36. Note that some people feel that predictions of dire labor shortages are overblown; yet, it is clear that some industries will be more hard-pressed for labor than others. A good discussion of this can be found in Ed Fraumeni, *Face of the Future*, WORKFORCE MGMT., Oct. 9, 2006, at 1.

37. NAT'L FED. INDEP. BUS., NAT'L SMALL BUSINESS POLL: THE CHANGING SEARCH FOR EMPLOYEES 1 (2001), <http://www.411sbfacts.com/files/changingsearchemployees.pdf>.

38. Vivek Wadwa, AnnaLee Saxenian, Ben Rissing, & Gary Gereffi., *America's New Immigrant Entrepreneurs: Part I* 11 (Duke Univ. Sci., Tech., & Innovation, Paper No. 23, 2007), available at http://people.ischool.berkeley.edu/~anno/Papers/Americas_new_immigrant_entrepreneurs_I.pdf.

39. See Carl Schramm & Robert E. Litan, *The Growth Solution*, AMERICAN, July-Aug. 2008, at 32.

40. THOMAS FRIEDMAN, *THE WORLD IS FLAT: A BRIEF HISTORY OF THE TWENTY-FIRST CENTURY* (2005).

trade barriers.⁴¹ Government can also help ensure that trade laws are enforced.

Recently, the National Association of Manufacturers released studies on the structural costs of lowering manufacturing costs in the United States compared with its trading partners.⁴² They found that United States manufacturers pay 31.7% 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.⁴³ United States 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).⁴⁴

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 lower cost, firms can more effectively compete on price while focusing domestic production efforts in other areas.⁴⁵ To 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.⁴⁶

41. For more information on small business opportunities and exports, see Chad Moutray & Kathryn Tobias, *Profile of Small Businesses and International Trade, in REPORT TO THE PRESIDENT 2008*, *supra* note 22, at 67.

42. See THE MFG. INST. & MFRS. ALLIANCE/MAPI, *THE TIDE IS TURNING: AN UPDATE ON STRUCTURAL COST PRESSURES FACING U.S. MANUFACTURERS* (2008).

43. JEREMY A. LEONARD, NAT'L ASS'N OF MFRS., *HOW STRUCTURAL COSTS IMPOSED ON U.S. MANUFACTURERS HARM WORKERS AND THREATEN COMPETITIVENESS 1* (2003), http://www.nam.org/~media/Files/s_nam/docs/227600/227525.pdf.ashx; JEREMY A. LEONARD, NAT'L ASS'N OF MFRS., *THE ESCALATING COST CRISIS: AN UPDATE ON STRUCTURAL COST PRESSURES FACING U.S. MANUFACTURERS 2* (2006), http://www.nam.org/~media/Files/s_nam/docs/237500/237456.pdf.ashx.

44. THE MFG. INST., NAT'L ASS'N OF MFRS. & RSM McGladrey, *The Future Success of Small and Medium Manufacturers: Challenges and Policy Issues 7* (2006), http://www.rsmmcgladrey.com/Knowledge-Center/Downloads/SMM-Report/smm_report.pdf.

45. See generally STRATEDGE, U.S. SMALL BUS. ADMIN., *OFFSHORING AND U.S. SMALL MANUFACTURERS* (2008), <http://www.sba.gov/advo/research/rs336tot.pdf>.

46. *Id.* at 4, 68-69.

II. OPPORTUNITIES

This section will outline five opportunities that small businesses will hopefully pursue in the next decade. These include (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.

A. *Increasing Investments in Technology and Innovation*

Many economic development officials are seeking the “next big thing” that will drive their 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,⁴⁷ and governments now regularly promote technology transfer as an important component of economic development.⁴⁸ Furthermore, regions with greater entrepreneurial growth have been associated with higher levels of innovation and technology use,⁴⁹ and states that promote new firm formation through public policy are more likely to experience higher employment, incomes, and overall output.⁵⁰ Therefore, policymakers of both political parties understand that risk-taking entrepreneurs have a positive impact on regional economic development.⁵¹

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 United States Small Business Administration’s Office of Advocacy shows that forty percent of the companies that issued at least fifteen

47. BJK ASSOCS., U.S. SMALL BUS. ADMIN., *THE INFLUENCE OF R&D EXPENDITURES ON NEW FIRM FORMATION AND ECONOMIC GROWTH 2* (2002), <http://www.sba.gov/advo/research/rs222tot.pdf>.

48. Scott Shane, *Government Policies to Encourage Economic Development Through Technology Transfer*, in *THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 103* (2004), http://www.sba.gov/advo/research/sb_econ2004.pdf.

49. S. MICHAEL CAMP, U.S. SMALL BUS. ADMIN., *THE INNOVATION-ENTREPRENEURSHIP NEXUS: A NATIONAL ASSESSMENT OF ENTREPRENEURSHIP AND REGIONAL ECONOMIC GROWTH AND DEVELOPMENT 5* (2005), <http://www.sba.gov/advo/research/rs256tot.pdf>.

50. BRUCE ET AL., *supra* note 18, at 22.

51. See Chad Moutray, *Recent Research Uncovers Multifaceted Relationship of Entrepreneurship and Local Economic Growth*, SMALL BUS. ADVOC. (U.S. Small Bus. Admin., Office of Advocacy, D.C.), Feb. 2007, at 6, <http://www.sba.gov/advo/feb07.pdf>.

patents over a five-year period were small businesses.⁵² In addition, these small firms produced significantly more patents per employee than the larger firms in the sample.⁵³ 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 “[s]mall 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 unit.”⁵⁴ That study identifies emerging industries that favor small businesses, including: imaging and display, nanotechnology, photonics and optical components, and biomedical and biotechnology pipeline firms.⁵⁵ 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.⁵⁶ 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.⁵⁷

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.⁵⁸ Among its conclusions, it stated that:

52. ANTHONY BREITZMAN & DIANA HICKS, U.S. SMALL BUS. ADMIN., AN ANALYSIS OF SMALL BUSINESS PATENTS BY INDUSTRY AND FIRM SIZE 5 (2008), <http://www.sba.gov/advo/research/rs335tot.pdf>.

53. *See id.* at 6-7.

54. *Id.* at v.

55. *Id.* at vi.

56. *See, e.g.*, CHI RESEARCH, INC., U.S. SMALL BUS. ADMIN., SMALL SERIAL INNOVATORS: THE SMALL FIRM CONTRIBUTION TO TECHNICAL CHANGE (2003), <http://www.sba.gov/advo/research/rs225tot.pdf>; William Baumol, *Small Firms: Why Market-Driven Innovation Can't Get Along Without Them*, in THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 183 (2005), http://www.sba.gov/advo/research/sb_econ2005.pdf.

57. JONATHAN T. ECKHARDT & SCOTT SHANE, U.S. SMALL BUS. ADMIN., INNOVATION AND SMALL BUSINESS PERFORMANCE: EXAMINING THE RELATIONSHIP BETWEEN TECHNOLOGICAL INNOVATION AND THE WITHIN INDUSTRY DISTRIBUTIONS OF FAST GROWTH FIRMS 1 (2006), <http://www.sba.gov/advo/research/rs272tot.pdf>.

58. MILT STEWART, U.S. SMALL BUS. ADMIN., SMALL BUSINESS & INNOVATION: A REPORT OF AN SBA OFFICE OF ADVOCACY TASK FORCE (1979).

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.⁵⁹

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.

B. *Grooming Local Entrepreneurs for Growth (“Economic Gardening”)*

Policymakers eager to show that they are bringing jobs to their district or their state have many options. There are two schools of thought among economic developers—“economic hunting” and “economic gardening.”⁶⁰ Economic hunting is a strategy that is often pursued by offering of generous incentives to lure large businesses.⁶¹ Success can bring a lot of publicity and ultimately a number of high-quality employment opportunities for the area. That said, not everyone wins at the game of “chasing smokestacks.” Some regions will never be able to outbid others for these high-profile acquisitions of firms and jobs.

Economic gardening is an alternative strategy that grooms existing small businesses for growth. Chris Gibbons—the Director of Business & Industry Affairs for the city of Littleton, Colorado, and a champion of “economic gardening”—argues that if communities plowed the dollars spent on luring big businesses into promotion of local small businesses, the payoff could be greater.⁶² Convincing policymakers to think long term instead of in political cycles, though, can often be a hard sell.⁶³

59. *Id.* at app. 1, iii.

60. Steve Quello & Graham Toft, *Economic Gardening: Next Generation Applications for a Balanced Portfolio Approach to Economic Growth*, in *THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT*, 157 (2006), http://www.sba.gov/advo/research/sb_econ2006.pdf [hereinafter *REPORT TO THE PRESIDENT 2005*]

61. *See id.* at 168.

62. *Id.* at 169.

63. *Id.* at 157.

C. 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 12.3% in the second quarter of 2008, and these figures have risen steadily, outpacing the growth in imports, since 2005.⁶⁴ 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.⁶⁵ These companies constituted 97.3% of all known exporters, and they engaged in \$260 billion in known transactions—28.9% of the total.⁶⁶ 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. 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 complicate matters by 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.⁶⁷ Businesses that did engage in international trade often did so based on inquiries instead of a strategic initiative, or by becoming subcontractors with larger firms who were engaged internationally.⁶⁸

64. See QUARTERLY INDICATORS—SECOND QUARTER 2008, *supra* note 4, at 1.

65. Chad Moutray & Kathryn Tobias, *Profile of Small Businesses and International Trade*, in REPORT TO THE PRESIDENT 2008, *supra* note 22, at 73.

66. See *id.*

67. See PALMETTO CONSULTING, INC., U.S. SMALL BUS. ADMIN., COSTS OF DEVELOPING A FOREIGN MARKET FOR A SMALL BUSINESS: THE MARKET & NON-MARKET BARRIERS TO EXPORTING BY SMALL FIRMS (2004), <http://www.sba.gov/advo/research/rs241tot.pdf> (discussing small firm barriers to exporting imposed by forces both in the market and outside the market).

68. *Id.*

D. *Promoting Entrepreneurship Among Women, Minorities, Veterans, and Immigrants*

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.⁶⁹ While the profiles of those pursuing self-employment are varied, studies show that those individuals who opt to work for themselves are more likely to be older white males with greater overall wealth.⁷⁰ 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. The number of women-owned employer firms increased 8.3% between 1997 and 2002 (the year of the most recent economic census), with women-owned firms totaling 6.5 million or 28.2% of the total.⁷¹ 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% of the total number of businesses, and Hispanic-owned firms constituted the largest portion owned by a single minority group with 6.6% of all U.S. firms.⁷² 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,⁷³ suggesting that Americans should embrace the influx of new citizens to its shores. Moreover, where differences do exist between native-born and im-

69. See TIMOTHY BATES, *RACE, SELF-EMPLOYMENT, AND UPWARD MOBILITY: AN ILLUSIVE AMERICAN DREAM* (1997); Ying Lowrey, *Business Density, Entrepreneurship, and Economic Well-Being*, Working Paper (2004), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=744804.

70. Chad Moutray, *Educational Attainment and Other Characteristics of the Self-Employed: An Examination Using Data from the Panel Study of Income Dynamics 14* (U.S. Small Bus. Admin., Working Paper No. 313, 2007), <http://www.sba.gov/advo/research/rs313tot.pdf>.

71. YING LOWREY, U.S. SMALL BUS. ADMIN., *WOMEN IN BUSINESS: A DEMOGRAPHIC REVIEW OF WOMEN'S BUSINESS OWNERSHIP 5* (2006), <http://www.sba.gov/advo/research/rs280tot.pdf>.

72. YING LOWREY, U.S. SMALL BUS. ADMIN., *MINORITIES IN BUSINESS: A DEMOGRAPHIC REVIEW OF MINORITY BUSINESS OWNERSHIP 6-7* (2007), <http://www.sba.gov/advo/research/rs298tot.pdf>.

73. See *supra* text accompanying note 38.

migrant self-employment rates, these can often be explained by financial, human capital, and legal barriers.⁷⁴

Another group that will receive more attention in the coming years is the veterans' community, including those who were disabled in service. With the United States 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 of veterans is anything like its predecessors, it will be highly entrepreneurial. Past research, for instance, shows that military service is a major determinant of self-employment, and veterans experience higher self-employment rates than non-veterans.⁷⁵ One study suggested that 22% of veterans in the population were purchasing or starting a new business or considering it.⁷⁶ In 2002, veteran-owned firms represented 14.5% of the total respondent business owners to the United States Census Bureau's Survey of Business Owners (or 12.2% of the respondent firms).⁷⁷ Policy-makers should find ways to promote greater business ownership among veterans, women, and minorities in the coming years.

E. *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 links 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.⁷⁸ Along those lines, regions

74. Robert W. Fairlie & Christopher Woodruff, *Mexican-American Entrepreneurship* 15-27 (Hudson Inst. Ctr. for Employment Policy, Paper No. 06-03, 2006), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=907681.

75. ROBERT W. FAIRLIE, U.S. SMALL BUS. ADMIN., SELF-EMPLOYED BUSINESS OWNERSHIP RATES IN THE UNITED STATES: 1979-2003, AT 5 (2004), <http://www.sba.gov/advo/research/rs243tot.pdf>; Moutray, *supra* note 70, at 14.

76. WALDMAN ASSOCS. & REDA INT'L, U.S. SMALL BUS. ADMIN., ENTREPRENEURSHIP AND BUSINESS OWNERSHIP IN THE VETERAN POPULATION 8 (2004), <http://www.sba.gov/advo/research/rs242tot.pdf>.

77. Jules Lichtenstein & Joseph Sobota, *Characteristics of Veteran Business Owners and Veteran-Owned Businesses*, in THE SMALL BUSINESS ECONOMY: A REPORT TO THE PRESIDENT 119, 124 (2007), http://www.sba.gov/advo/research/sb_econ2007.pdf.

78. See RICHARD FLORIDA, THE RISE OF THE CREATIVE CLASS: AND HOW IT'S TRANSFORMING WORK, LEISURE, COMMUNITY, AND EVERYDAY LIFE (2002); Yannis Georgellis & Howard J. Wall, *What Makes a Region Entrepreneurial?: Evidence from Britain*, 31 ANNALS REGIONAL SCI. 385 (2000); Edward L. Glaeser, *Are Cities Dying?*, 12 J. ECO. PERSP. 139 (1998); SAM YOUL LEE, RICHARD FLORIDA & ZOLTAN ACS, *Creativity and Entrepreneurship: A Regional Analysis of New Firm Formation*, 38.8 RE-

with greater educational levels also tend to have reduced poverty.⁷⁹ Greater educational attainment means increased incomes and various opportunities. For the purposes of this Article, there are strong links 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 collegiate experience also play into the employment decision.⁸⁰

Small businesses are often the first employers of many Americans, and these workers are often less educated than the rest of the population.⁸¹ As a result, small businesses must devote significant resources to training their workforce.⁸² 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.⁸³ 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 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 of promoting innovation. Universities, especially since passage of the Bayh-Dole Act of 1980,⁸⁴ aggressively push “technology transfer” programs whereby academically sponsored research leads to new commercialized ventures in the community.⁸⁵ This phenomenon—

GIONAL STUDIES 879 (2004), available at [http://creativeclass.com/rfcgdb/articles/Creativity%20and%20Entrepreneurship,%20A%20Regional%20\(Lee,%20Florida,%20Ac\).pdf](http://creativeclass.com/rfcgdb/articles/Creativity%20and%20Entrepreneurship,%20A%20Regional%20(Lee,%20Florida,%20Ac).pdf).

79. See STEPHAN J. GOETZ, THE PLACE-BASED STRUCTURAL DETERMINANTS AND EFFECTS OF SELF-EMPLOYMENT 6, 7 (2006), http://nercrd.psu.edu/Publications/rdp_papers/rdp33.pdf (noting that self-employment has a positive correlation with escaping from poverty, and also that there is a positive correlation between education and self-employment). See generally BATES, *supra* note 69.

80. Moutray, *supra* note 70, at 3; Mark Weaver, Pat Dickson & George Solomon, *Entrepreneurship and Education: What is Known and Not Known About the Links Between Education and Entrepreneurial Activity*, in REPORT TO THE PRESIDENT 2005, *supra* note 60, at 113.

81. See Jules Lichtenstein, *Small Business Training and Development*, in REPORT TO THE PRESIDENT 2008, *supra* note 22, at 107.

82. *Id.*

83. HOPE & MACKIN, *supra* note 32, at i.

84. Bayh-Dole Act, Pub. L. No. 96-517, 94 Stat. 3019 (1980) (codified as amended at 35 U.S.C. §§ 200-212 (2000)).

85. Shane, *supra* note 48, at 104.

where innovation provides the linkages for greater entrepreneurship—was discussed earlier, but it is further proof that investments in education can pay off.⁸⁶

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 provides 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. 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 would benefit from a business tax and regulatory environment that allows them to prosper without being overly burdened, and they worry about maintaining and attracting a quality workforce. The fact that smaller businesses are less able to provide the generous benefits of their larger counterparts makes the competition for talent that much harder.

86. See *supra* notes 47-59 and accompanying text.

The future for small business in the United States is very bright. Leadership from both political parties embraces policies that stimulate entrepreneurship and its contributions to our economy and to our competitive strength in the global marketplace. This Article has outlined some of the opportunities and challenges that await small business owners. Clearly, there are many others that I could have highlighted. 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.