

# SMALL BUSINESS

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# RESEARCH BULLETIN

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## *The Small Business Economy 2002-2003*

### A Report to the President with Data from 2001-2002

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This report looks at small business economic data for the years 2001 and 2002. Small businesses have important roles in the economy, responding to demand for new products and services, employing half of private sector workers, and creating most of the net new jobs. In the economic life cycle, small businesses are often the beginnings of large businesses. Small and large businesses often work together, taking risks and building on each other's innovations to generate economic growth. Small firms change market structure, and when market demand fluctuates, they also act as shock absorbers by using flexible production techniques.

#### **The Small Business Economy in 2001-2002**

The Information Revolution, the latest technological challenge for small businesses, has slowed in recent years after two decades of growth that affected the economy overall. The technology slowdown affected the NASDAQ stock market by March 2000, while the overall economy experienced a downturn in 2001.

Economic troubles hit the labor market in both 2001 and 2002, but output in the economy increased over both years, reflecting continuing increases in productivity. The number of employers and the self-employed declined slightly, by 0.6 and 1.8 percent, respectively, over the 2001-2002 period. The unemployment rate climbed, but inflation remained low. Small firms as a group held their ground, reflected in the relatively stable numbers of both employer firms and self-employed individuals.

The year 2002 set the stage for recovery. While the technology gains remained, it was unclear whether the Information Revolution of recent decades had run its course.

Small business and other economic data indicate that the economy was as much flat as in a downturn in 2001-2002.

#### **The Financial Markets for Small Firms**

The recession of 2001, which ended in the third quarter, was relatively mild with respect to declines in gross domestic product, but the pace of recovery was slow. Consumer spending and household investment, as well as federal, state, and local government deficit spending continued to support the economy. The collapse of business spending led the recession in 2001, caused in part by over-investment in the late 1990s. While the decline in corporate profits ended and reversed after the last quarter of 2001, corporate profits remained at a low level, and capacity utilization in the manufacturing sector remained low.

The Federal Reserve Board maintained a steady, but very easy monetary policy throughout most of 2002 after 10 rate cuts in 2001, and lowered the discount rate one more time in November 2002 to stave off potential deflation. Short- and intermediate-term interest rates stabilized throughout most of 2002, then moved downward after the rate cut. Interest rates paid by small firms moved, with a time lag, in line with overall interest rate movements in the capital and credit markets.

Most banks reported continued weakness in demand for commercial and industrial loans, despite less tightening in credit standards and terms. Nevertheless, profitability at U.S. commercial banks was at historic highs as income from rising interest margins and home-mortgage-related lending surpassed rising default-related losses. Small business lending by banks showed moderate increases. For example, small business loans outstanding in loan

sizes under \$1 million grew 5.1 percent between June 2001 and June 2002, compared with an increase of 5.4 percent in the previous period, as both borrowers and lenders continued to hold off on new borrowing and lending.

Activities in the initial public offering market for smaller issuers almost disappeared in the 2001-2002 period. Angel investment, a type of venture investing that has been less sensitive to the changes in the IPO markets, also declined by 50 percent.

### **Federal Procurement from Small Firms 2001-2002**

The federal government awarded \$259.1 billion in contracts for the purchase of goods in FY 2002, up from \$242.6 billion in FY 2001. Small businesses were awarded \$54.1 billion (20.9 percent of the total) in direct prime contracts, up from \$53.9 billion (22.2 percent) in FY 2001. Small businesses as federal subcontractors were awarded \$34.4 billion in subcontracts in FY 2002. Prime contract and subcontract amounts together totaled \$88.4 billion in FY 2002, down about \$1 billion from \$89.4 billion in FY 2001. The prime and subcontracting dollar totals represent a variety of goods and services provided by small businesses, including research and development, educational and training courses, paint, toiletries, military weapons, housing and hardware. These goods and services support federal civilian and military personnel around the world.

### **Minority- and Women-Owned Businesses**

Business ownership continues to be an important means by which Americans, including women, minorities, and immigrants, have been able to enter the economic mainstream. A variety of data sources are used to examine business ownership by these groups; current year data are generally not available because of time lags in extracting the data.

Minority business ownership doubled from 7 percent in 1982 to almost 15 percent in 1997, the latest year for which Census data are available. Minorities also made important financial contributions to the U.S. economy, with payroll totaling \$95.5 billion in 1997.

Evidence indicates that business ownership is an effective means of improving the financial well-being of women. Three primary sources provide data on women in businesses: the Bureau of the Census, which produces data every five years in years ending in 2 and 7; the Bureau of Labor Statistics (BLS) which produces data monthly (although annual figures offer more detail), and the Internal Revenue Service, which produces figures annually. Women's self-employment increased from 1.76 million in 1976 to 3.75 million in 2000; their business ownership, according to Census data, increased from 6.40 million in 1992 to 7.45 million five years later; and their ownership of sole proprietorships increased from 5.6 million in 1990 to 7.1 million in 1998.

### **For More Small Business Information**

For the complete report, *The Small Business Economy 2002-2003*, visit the Office of Advocacy website at [www.sba.gov/advo](http://www.sba.gov/advo). Print copies are available from the U.S. Government online bookstore, <http://bookstore.gpo.gov>.

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