

The Small Business Economy 2008

Office of Advocacy, February 2009 [376 pages]

Purpose and Scope

In the latest edition of *The Small Business Economy*, the Office of Advocacy reviews the economic environment for small businesses in the year 2007, including the financial and federal procurement marketplaces. New research focuses on small businesses in international trade, training of workers in small businesses, tax policy, and business creation activities. Advocacy's annual report on implementation of the Regulatory Flexibility Act and the results of Advocacy's initiative to carry regulatory flexibility successes to the state level are summarized. Appendices provide data on small business.

Highlights

The Small Business Economy in 2007

Small businesses, like the rest of the economy in 2007, faced an economic slowdown. The economy experienced solid growth in the first and fourth quarters, but began and ended the year with real GDP up only slightly.

- Housing starts, which had increased rapidly since 1990, dropped to 1 million homes by December 2007.
- Exporting was among the stronger positive factors. Real exports rose 8.1 percent, while real imports increased 1.9 percent.
- Increases in service sector employment more than offset declines in goods-producing employment. The economy generated 1.1 million new jobs over the year.
- In the first quarter, 74 percent of net new jobs were in small firms with fewer than 500 employees. Third quarter data saw declining net job change in all firm size classes.
- Incorporated self-employment rose from 5.5 million in 2006 to 5.8 million in 2007; unincorporated self-employment fell from 10.6 million to 10.4 million.

Small Business Financing in 2007

The financial markets felt the effects of the decelerating housing market and increasing energy prices to some

extent in 2007. Large declines in home mortgage borrowing were offset by increased borrowing by governments and nonfinancial businesses. Business borrowing increased from \$791 billion in 2006 to \$1.046 trillion in 2007.

- Small business lending strengthened for all small business loan size categories through June 2007, particularly for loans of \$100,000 to \$1 million.
- Large lending institutions with assets of \$10 billion or more accounted for more than half of loans under \$100,000.
- The volume of initial public offerings increased. Angel investing was also up, by 12 percent, as 57,000 ventures received angel funding in 2007.

Federal Procurement from Small Firms

Small businesses continued to benefit from the federal acquisition of their goods and services.

- The Small Business Administration's recertification regulation went into effect June 30, 2007. It requires a small business holding a contract for more than five years to recertify its size status after the fifth year.
- Small firms were awarded \$83.3 billion in direct federal prime contracts in fiscal year 2007, up from \$77.7 billion in FY 2006. The small business share of the \$378.5 billion total available for small business competition was 22 percent.
- Small businesses also received \$64 billion in subcontracting dollars in FY 2007.
- The value of procurement awards to businesses owned by women, minorities, service-disabled veterans, and businesses in designated "HUBZones" increased in FY 2007.

Profile of Small Businesses and International Trade

A bright spot in the U.S. economy in 2007 was the increase in U.S. exports. Exporting by small firms has considerable room for growth. Behind the numbers is a portrait of U.S. competitiveness on world markets, which

has benefited in the past from investment in research and development.

- U.S. real exports were up by 7.9 percent over the 2006-2007 period, compared with a 2.2 percent increase in real GDP.
- Small businesses with fewer than 500 employees constitute 97.3 percent of identified U.S. exporters, less than their share of all businesses.
- The total known value of U.S. small business exports has increased, while the small business share has declined from 31.1 percent of the \$500.7 billion in known 1996 exports to 28.9 percent of the \$910.5 billion in exports in 2006.

Small Business Training and Development

As well as being primary job generators, small businesses are major trainers of U.S. employees.

- The small firm work force includes many entry-level workers. About two-thirds of workers get their first jobs in small firms; thus small firms train much of the work force.
- The training offered in small firms tends to be more general, informal, and flexible than that provided by large firms.
- The 1996, 2001, and 2004 Surveys of Income and Program Participation show declines in employer-provided training between 1996 and 2004—by 6.1 percentage points in small firms and 11.6 percentage points in large firms.

A Tax Policy Update for America's Small Businesses

Taxes are perennially a source of concern for small as well as large firms, and advances in data products have expanded the available knowledge about tax policies' effects.

- Federal tax policy issues include the disposition of the 2001 and 2003 income tax rates, the growing AMT filing population, depreciation rules, and carried interest.
- State and local tax policy issues include taxation of gross receipts instead of net profits, streamlining of state sales tax rules, decoupling of state tax rules from federal rules, and the determination of "nexus" for multi-state tax purposes.
- Emerging themes include the aging of the population, expanding technology for tax planning, and increasingly environmentally conscious tax policies.

Business Creation in the United States: Entry, Startup Activities, and the Launch of New Ventures

The Panel Study of Entrepreneurial Dynamics offers an opportunity to explore the initial stages of the business creation process as well as the outcomes—new firms.

- In 2005, more than 12 million people were involved in trying to start new firms.
- For 90 percent of new entrepreneurs, it takes more than five years for an outcome to be determined.
- Beginning entrepreneurs devoted an amount of time working on their startups equal to about 2.7 percent of all hours worked in 2005—equivalent to almost half the total work time of self-employed workers.
- The most important factors leading to success in the business creation process are knowledge of the industry and aggressive pursuit of the opportunity.

Regulatory Flexibility Act Implementation, FY 2007

The Office of Advocacy oversees implementation of the Regulatory Flexibility Act, an important tool requiring federal agencies to review the potential effects of proposed regulations on small entities.

- As a result of the law's implementation in FY 2007, small businesses saved nearly \$3 billion in first-year and annually recurring costs.
- Advocacy's Regulatory Review and Reform (r3) initiative, begun in FY 2007, was designed to address the RFA's section 610 requirement to look at current regulations.
- The Office of Advocacy promoted model regulatory flexibility legislation for states beginning in 2002. By summer 2008, 42 states had regulatory flexibility initiatives under way.

Ordering Information

The full text of this report and summaries 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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