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Small Businesses and the Community: Their Role and Importance Within a State's Economy

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Small Businesses and the Community: Their Role and Importance Within a State's Economy

Abstract

As communities focus on economic development, the common response has been the recruitment of outside industry. Left out has been the support for existing micro businesses and entrepreneurs. The research reported here explored the contributions of these smallest of the small business within the economy. For the study, 1,224 Oklahoma households were included. The research found that more than one in every five households owned and operated such a business. These businesses generated substantial gross income and employed at least one other person. These findings support including micro businesses in a comprehensive economic development plan.

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Introduction

As communities focus on local economic development efforts, one common response is to key on business and industry attraction or "smokestack chasing." Every community wants the next big large employer. Left out or given minimal attention in many of these economic development plans is support for existing micro businesses, those that employ fewer than 10 employees or are sole proprietorships. These businesses call the community "home" and may be on Main Street, on the outskirts, or a farm/ranch operation. One reason for the lack of attention to micro businesses often stems from a perception that they generate little in terms of jobs and dollars for the community's economic engine.

The purpose of the research reported here was to evaluate micro business contributions to a community's economic engine. The evaluation includes an analysis of the impact of micro businesses overall and as divided among urban, micropolitan, and other areas. Suggestions for the further development of the micro business segment are offered. The goal is to increase awareness and support for this business segment among Extension educators, community/economic development specialists, local leaders, and community members.

Review of Literature

Small businesses, most often defined using the Small Business Administration's definition of "fewer than 500 employees" (Small Business Administration, 2001), are well recognized worldwide as vital and significant contributors to economic development, job creation, and the general health and welfare of economies (Korsching & Allen, 2004; Morrison, Breen, & Ali, 2003). Yet the citizens of smaller towns and rural communities often define "small" far differently. They see a business with 50 to 100 employees as "big" business. A solution is to divide the "small" category into various subcategories. One subcategory is the micro business, a firm that employs fewer than 10 people (Devins, 1999).

Micro businesses form a dynamic, integral part of the market economy, providing goods and services and a gateway by which millions enter the economic and social mainstream of American society (Sexton, 1999). U. S. micro businesses accounted for 94% of all firms and 84% of employer firms. They employ up to 25% of all individuals or over 11% of all employees within employer-only firms (Family Economics and Nutrition Review, 2001; U. S. Census, 2001).

By 2002, 50.1% of the USA's 112.4 million private-sector workers were employed by micro business firms. In one substantially rural state, 77% of firms are micro in size, and they employ 13% of all workers (Small Business Administration, 2001). In the boom 80's, micro businesses generated the majority of new job growth. They continued that role during the slow down of the 1990's. Not only did they absorb all of the jobs that big businesses cut but, in fact, added 225,000 workers (Hopkins, 2005; Small Business Administration, 2004).

Yet for all of the positives surrounding micro businesses and their contributions, there are unanswered questions about them. Three research questions are addressed in the study reported here. First, what is the prevalence rate of micro businesses within a state, and what is the most common type of businesses found?

A related question is if the prevalence rate differs among metropolitan areas, micropolitan areas, and other areas, often labeled incorrectly as rural (Barta, 2003; U. S. Census Bureau, 2005). By the U. S. Census Bureau (2005), metropolitan areas, in the 2000 census, have an urbanized area of 50,000 or more inhabitants; micropolitan areas have an urban cluster of 10,000 to 49,999 inhabitants; and "other" areas are those that do not fit into either of the other two categories.

The third research question looked at two broad indicators of business contribution to the local community in terms of the number of people employed and gross income generated, thus expanding on the work of Muske and Woods (2004). This last question may offer information to local community leaders as to contributions to the community.

Methodology

Even though the numbers and contributions of micro businesses sound significant, it is suspected that many such businesses are missed in research studies. Typically business research draws from a business sampling frame only. Winter, Fitzgerald, Heck, Haynes, and Danes (1998) confirmed this in a study of family businesses of which many micro businesses are a part. To overcome this problem, Winter, et al. (1998) suggested using a household sampling frame and asking if the household owns a business.

For this study, the survey sample consisted of all households within Oklahoma that were included in Oklahoma telephone exchanges. Business phone numbers were excluded from the sampling frame. A computer-based questionnaire for the study was developed and pre-tested with micro business owners for accuracy and completeness. Using random digit dialing, households were contacted by telephone through the OSU Bureau of Social Research. In the fall of 2002, 1,224 household surveys were obtained, a 32% response rate.

Three screening questions were asked. The first question asked if the household owned a business. If yes, a second question asked if a member of the household was also involved in managing the business. Again if a positive answer was received, the last question asked was the number of people employed by the business. If the business employed 10 or fewer employees, a set of questions about the business was asked, and various demographic information was also gathered. Businesses were classified as being located in one of three location categories, metropolitan, micropolitan, and other. Frequencies and percentages were calculated and chi-square analysis, ANOVA and T-tests, based on data type, were used to determine variable significance.

Results

Overall, 221 of the 1,224 respondent households indicated that a business was owned and operated by the household, an 18% frequency rate (Table 1). The rate of business ownership was slightly less in metropolitan areas, 16.9%, and slightly higher in other areas (22.2%), but the differences were not statistically significant. Among the business owners, 68% were considered to be family businesses, with 69% of them based at home and 49% involving both spouses.

Table 1.
Micro Business Prevalence--Households Where a Member Owns and Runs a
Business Employing 10 People or Fewer

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	Ownership % of All Households	# of Households	N
Overall	18.1%	221	1224
Metropolitan areas	16.9%	130	769
Micropolitan areas	18.3%	46	252
Other (Rural) areas	22.2%	45	203

The most common businesses operated were service businesses (25.1%). Businesses related to agriculture, forestry, fishing, and hunting were second (20.9%), with retail stores third at 15.2% (Table 2).

Table 2.
Classification of Type of Business Operated

Business Type	Overall %	Metropolitan %	Micropolitan %	Other (Rural) %
Agriculture, forestry, fishing, & hunting	20.9	11.1	24.4	45.5
Construction	12.3	14.3	7.3	11.4
Manufacturing & mining	4.7	4.0	4.9	6.8
Transportation, communication & utilities	6.6	8.7	4.9	2.3
Wholesale	3.3	4.0	2.4	2.3
Retail	15.2	14.3	22.0	11.4
Finance, insurance & real estate	11.8	11.9	12.2	11.4
Services	25.1	31.7	22.0	9.1

The differences in type of business found in each location were significantly different ($X^2 = 31.868$, $df = 14$, $p = .004$). In metropolitan areas, service businesses were the most common (31.7%), while agriculture businesses were the most common in micropolitan areas (24.4%) and other areas (45.5%).

Table 3 looks at what micro businesses offer to the community. Two measures were used, the number of jobs the business provides and gross business income. While neither is a perfect measure of contributions, they provide insight into the business and are questions that owners to which owners will respond. If the study were focused on the well-being of the family, net income might be a better measure. However, considering the economic concept of the "multiplier effect," all income generated by a business will in some form be returned to the economy.

Overall micro business owners reported a mean gross business income of nearly \$136,000 and employed 2.34 workers. Thirty-six percent of the businesses indicated they had only one employee, the owner-manager. Gross income ranged from \$0 for 13% of the businesses to \$3,000,000 for one business. This high income level for one business means that income figures must be viewed cautiously. With mean income for all businesses over \$135,000 and median income only \$38,000, nearly \$100,000 less, most of the business owners reported income levels much lower than the mean (Table 3).

Table 3.
Micro Businesses Gross Income and Employment Numbers

	Overall	Metropolitan	Micropolitan	Other
Business Type	# emp.	# emp.	# emp.	# emp.
Overall				
Gross business income	\$135,935	\$135,692	\$108,129	\$163,300
# of employees	2.34	2.12	2.70	2.62
Agriculture, etc.				
Gross business income	\$123,962	\$500,000	\$23,240	\$40,583

# of employees	2.34	2.43	2.00	2.45
Construction				
Gross business income	\$49,200	\$51,429	\$35,000	\$48,500
# of employees	2.50	2.61	1.67	2.60
Manufacturing & mining				
Gross business income	\$856,750	\$1,625,000 NR	\$88,500	
# of employees	2.60	3.00	1.5	2.67
Transportation, etc.				
Gross business income	\$93,300	\$93,300	NR	NR
# of employees	2.43	2.45	3.00	1.00
Wholesale				
Gross business income	\$256,667	NR	\$750,000	\$20,000
# of employees	3.57	3	6.00	4.00
Retail				
Gross business income	\$119,700	\$85,833	\$207,333	NR
# of employees	2.41	1.72	3.67	2.60
Finance, etc.				
Gross business income	\$258,500	\$59,111	\$85,000	\$2,400,000
# of employees	2.28	1.33	4.00	3.40
Services				
Gross business income	\$40,511	\$42,888	\$26,250	NR
# of employees	2.15	2.03	2.44	2.75
NR - No response				

Although income averages were widely dispersed with other finance, real estate, and insurance businesses reporting income of \$2.4 million dollars (n=5) to \$20,000 for wholesale businesses located in the other location, these differences were not significant. On average, other reported the highest gross business income at just over \$163,000, with micropolitan reporting the lowest at slightly over \$108,000. This finding is in contrast to Gorodesky and McCarron (2003) and Levy and Weitz's (2001) findings that small-to-medium sized, non-urban other businesses would have lower income.

The average number of employees was found to be 2.34 employees and was significantly different between locations ($X^2 = 20.04$, $df = 10$, $p = .029$). Finance, real estate, and insurance businesses in micropolitan areas had the largest average (4), with other (rural) transportation businesses having the smallest (1).

Discussion and Conclusion

The research suggests that micro business play a crucial role in a community's economic system. The importance begins with the fact, found across all locations, that at a minimum one in every six households owns and operates such a business. Micro businesses employ local citizens and are an economic engine that causes cash to move through the community's economy. Successful local businesses allow owners to remain in place and generate opportunities for in-migration and more opportunities for other entrepreneurs.

So what should local communities do? Based on the data presented, economic development efforts need to include an effort to build the local economy through development of these resources, i.e., local businesses, already in place (ICMA, 2005). As mentioned earlier, this idea is often forgotten, and instead most economic development activities focus on business attraction and retention.

Probably the first element in this effort is finding one or more key local leaders, termed "sparkplugs" by some authors, willing to develop and move local economic development forward. One such person can be the Extension educator. The educator is uniquely placed and often recognized as providing applied research-based solutions to local problems. He or she is aware of existing local leadership, has a sense for other community members with a desire for leadership roles, is trained in the team approach, and is local. More and more development experts are recognizing that the answer to local problems comes from local people.

Once the decision is made to help develop existing businesses, three key steps must be taken. The first step, and perhaps the most effective, would be the identification of all of the businesses that exist within a community. Most communities would find it difficult to identify the potentially 18% of

households that operate a business and what that business is. Second, the needs and issues of local business owners must be identified (Muske & Woods, 2004). Third, communities need to identify available resources, local, regional, state, and national, that can work with the business owner. This means getting on the phone or Internet and bringing help to the community and not taking "no" for an answer.

Often the help comes from many different agencies, each of which has a part, often overlapping in type and area of coverage. Again, the local community can help by developing local ombudsmen who understand the programs available and then make the necessary connections between owner and available services (Lowe & Talbot, 2000). Other ideas can be found in the works of Muske and Woods (2004); Nolan (2003); Lyons (2003); Koven and Lyons (2003); Bradshaw and Blakely, (1999); Lichtenstein and Lyons, (2001); and Devin (1999).

Today, effective community economic development rarely wins with smokestack chasing or capturing the next "gazelle" (Chun & Griffin, 1996), but instead is achieved by making local decisions to use existing resources (the local businesses). The development must look at both the breadth and depth of the business community.

A diversity of businesses becomes the soil from which the next step is to grow a "critical mass" within a certain area (Bradshaw & Blakely, 1999). At that point, the critical mass can follow the suggestions of Lichtenstein and Lyons (2001) of taking a systemized approach customized to each community by drawing on that communities identified strengths and resources. Along with the critical mass, an interlocking network of support for each other, for prospective entrepreneurs and for the local community is helpful.

Extension can play a key role in each and every step towards such efforts and may be the "glue" that holds the system together. The local Extension office can be a key player in both identifying the small business community and providing education and support to further develop the segment of the local economy.

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