

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-0515

To: Members, Committee on Small Business
From: Committee Staff
Date: November 13, 2015
Re: Full Committee Hearing: *National Entrepreneurs' Day*

On Tuesday, November 17, 2015, at 11:00 am in Room 2360 of the Rayburn House Office Building, the Committee on Small Business will meet for the purpose of receiving testimony on the benefits of entrepreneurship to the American economy in conjunction with H.Res. 511, which expresses support for designation of the Third Tuesday of November as “National Entrepreneurs’ Day.” The hearing will examine methods utilized and cultivated by entrepreneurs to achieve prosperity, such as capitalizing on emerging industries and fostering innovation. The hearing will also examine the challenges present in today’s economy which may affect an entrepreneur’s ability to succeed.

I. Introduction

According to economists, the United States experienced an economic recession from December 2007 through June 2009.¹ This recession, often referred to as the “Great Recession,” lasted 18 months and was the longest recession experienced in the United States since World War II.² Since that time, America has experienced significant economic challenges, including high unemployment levels³ and a stagnant economy that has yet to rebound in a truly meaningful way especially due to the reduction in so-called “business dynamism.”⁴

In a flexible, non-stagnant economy there are “opportunities for businesses to enter the market or expand, but it also allows businesses to fail or contract.”⁵ However, the rate of new business creation has dropped by nearly fifty percent since 1978.⁶

¹ <http://www.nber.org/cycles/sept2010.pdf>. It is important to note this organization is not affiliated with the federal government.

² *Id.*

³ The unemployment rate topped 10 percent in October 2009. It remained above 9 percent for 30 months. BUREAU OF LABOR AND STATISTICS, LABOR FORCE STATISTICS FROM THE CURRENT POPULATION SURVEY (Aug. 2014), available at <http://data.bls.gov/timeseries/LNS14000000>.

⁴ Binyamin Appelbaum, *U.S. Economic Recovery Looks Distant as Growth Stalls*, N.Y. TIMES, June 11, 2014, available at http://www.nytimes.com/2014/06/12/business/economy/us-economic-recovery-looks-distant-as-growth-lingers.html?hp&_r=1; accord INTERNATIONAL MONETARY FUND, WORLD ECONOMIC OUTLOOK: CRISIS AND RECOVERY 110-111 (2009), available at <https://www.imf.org/external/pubs/ft/weo/2009/01/pdf/c3.pdf> (noting that on average recessions last for a year and the economy typically recovers to peak output in less than a year).

⁵ Rob Grunewald, *A Dynamic Economy Means Churning Employment*, FEDGAZETTE, Mar. 1, 2005, available at https://www.minneapolisfed.org/publications_papers/pub_display.cfm?id=1532&.

⁶ IAN HATHAWAY, MARK E. SCHWEITZER, AND SCOTT SHANE, FEDERAL RESERVE BANK OF CLEVELAND, THE SHIFTING SOURCE OF NEW BUSINESS ESTABLISHMENTS AND NEW JOBS 2 (2014), available at

Business dynamism – where “firms continually are born, fail, expand, and contract,”⁷ – is an “inherently disruptive”⁸ process that is critical to long-term economic growth and the health of the economy.⁹ Frequently, business dynamism also is referred to as creative destruction.¹⁰ In a dynamic economy, newer, more efficient processes and technologies supplant older, less efficient processes and technologies. Often, these technological developments are spearheaded by new firms competing with older established firms utilizing older technologies. Overtime, the new firms gain market share from the older firms who either must invest in the new technology to stay competitive or eventually exit the market. One result of this process is a shift in employment from older firms to newer firms.¹¹

The data on new firm creations already cited in this memorandum shows a decline in business dynamism during the past three decades but a significant drop off since 2006.¹² Notably, for the first time in over 30 years, the number of business deaths exceeds the number of business births.¹³ As the United States fails to engage in this dynamic cycle of business birth and death, there is a significant reduction in job creation which perforce contributes to a weakened economy.

II. Who Is an Entrepreneur?

While the terms small business, startup, and entrepreneur are sometimes used interchangeably, entrepreneurs tend to encompass a larger group of individuals. Merriam-Webster defines an entrepreneur as “a person who starts a business and is willing to risk loss in order to make money” or as “one who organizes, manages, and assumes the risks of a business or enterprise.”¹⁴ Another source defines an entrepreneur as “one who creates a new business in the face of risk and uncertainty for the purpose of achieving profit and growth by identifying opportunities and assembling the necessary resources to capitalize on those opportunities.”¹⁵

<http://www.clevelandfed.org/research/commentary/2014/2014-15.pdf>. In 1978, there were 12 new businesses created for each existing business while in 2011 there were only 6.2 new firms created for each established business.
Id.

⁷ IAN HATHAWAY & ROBERT E. LITAN, BROOKINGS INSTITUTION, DECLINING BUSINESS DYNAMISM IN THE UNITED STATES: A LOOK AT STATES AND METROS Abstract (2014), *available at* http://www.brookings.edu/~media/research/files/papers/2014/05/declining%20business%20dynamism%20litan/declining_business_dynamism_hathaway_litan.pdf.

⁸ *Id.* at 1-2.

⁹ *Id.* at 1-2.

¹⁰ *Id.* at 2.

¹¹ The primary economic benefit of business dynamism is “a more efficient allocation of goods and services relative to demand the resources required to produce them.” Grunewald, *supra* note 5. Further, this process allows “productivity gains by which more productive firms drive out less productive ones, new entrants disrupt incumbents, and workers are better matched with firms.” HATHAWAY AND LITAN, *supra* note 7, at 2. As a result of productivity gains, businesses may become more profitable, increase output, and have the capacity to hire new workers at increased wages. Thus, business dynamism leads to productivity gains which leads to increased employment at higher wages resulting in economic expansion.

¹² HATHAWAY AND LITAN, *supra* note 7, at 2.

¹³ *Id.* Unfortunately, the most recent data from 2013 sees this trend continuing.

¹⁴ <http://www.merriam-webster.com/dictionary/entrepreneur>.

¹⁵ NORMAN M. SCARBOROUGH & JEFFREY R. CORNWALL, ENTREPRENEURSHIP AND EFFECTIVE SMALL BUSINESS MANAGEMENT 5 (11th ed. 2015).

Given these definitions, it is clear that an entrepreneur may or may not be a business with employees and the firm may or may not make any revenue. Further, the concern may be a newly created firm or the business may have been running for several years – either way the individual who started that establishment and is overseeing its daily activities is an entrepreneur. Broadly, then an entrepreneur is anyone who assumes risk as part of a business venture and for purposes of this hearing that is the broad definition that will be used.

III. The State of Entrepreneurship

Entrepreneurs have always played a vital role in America. In 2014 entrepreneurship rose to its highest level in 16 years, indicating that entrepreneurship within the United States is continuing to grow.¹⁶ Despite economic instability and the decline in new firm creation, over 50 percent of the United States population believes that good opportunities exist for starting businesses.¹⁷ One reason for the disconnect between what appears to be a heightened desire to engage in entrepreneurship and the numbers regarding new firm creation may be that the statistics used may not accurately capture start-up activity, as frequently start-up firms do not have employees that a traditional small business would.¹⁸

Entrepreneurs provide an overall value to the economy by “target[ing] advanced industries, creat[ing] jobs, launch[ing] innovative products and services, and compet[ing] globally.”¹⁹ Among developed countries, the United States continues to have one of the highest entrepreneurship rates.²⁰ This may be due to the belief in the United States that being an entrepreneur is a viable and socially accepted career path. In America, 65% of the adult population believes that being an entrepreneur is a good career path and 77% believe entrepreneurs have high status.²¹ This differs from other countries which may not support the idea as a career path due to risk aversion or fear of failure.²²

Another reason for heightened entrepreneurship rates may be due to America’s innovative spirit. The United States remains one of the most innovative countries and according to a recent study exhibits a higher level of innovation than 28 other countries with innovation-driven economies.²³ The merger among innovation, new firms, and job creation is an established cycle, and is necessary to foster economic growth. Economic growth generally occurs in two

¹⁶ DONNA J. KELLEY ET AL., GLOBAL ENTREPRENEURSHIP MONITOR, 2014 UNITED STATES REPORT 7 (2015), available at <http://www.babson.edu/Academics/centers/blank-center/global-research/gem/Documents/GEM%20USA%202014.pdf>.

¹⁷ *Id.* at 8

¹⁸ *Id.* at 15.

¹⁹ *Id.* at 20.

²⁰ *Id.* at 17.

²¹ *Id.* at 26.

²² For example, in Germany risk aversion puts them at a disadvantage to entrepreneurship. <http://www.gemconsortium.org/country-profile/64>. Whereas in South Korea fears of failure may prevent one from becoming an entrepreneur. <http://www.gemconsortium.org/country-profile/125>.

²³ Kelley, *supra* note 16, at 21. Bloomberg’s Global Innovation Index ranked the United States the sixth most innovative country in 2015. While this still places the United States in the top 10 this is 5 spots down from 2013 when the United States was ranked first in this index. Compare <http://www.bloomberg.com/graphics/2015-innovative-countries/> with <http://www.bloomberg.com/slideshow/2013-02-01/50-most-innovative-countries.html#slide51>.

ways; through imitative growth which “occurs within the existing technological frontier,”²⁴ or through innovative growth which “pushes that frontier outward.”²⁵ Examples of imitative growth include “capital accumulation, expansion and upgrading of the labor force, and adaption of ideas elsewhere.”²⁶ Innovative growth occurs with “the development of new products and new production processes.”²⁷

For example in 2014, “professional, scientific, and technical services, nondurable goods manufacturing; real estate and rental and leasing where the leading contributors to real [United States] economic growth.”²⁸ These industries encompass both types of economic growth with technical services resulting in innovative growth, and established industries such as nondurable-goods manufacturing, requiring imitative growth to expand. As the array of industries above demonstrates, high levels of ingenuity and innovation enhance entrepreneurs’ ability to succeed.

IV. Conclusion

In recent years, while some economic obstacles may have restricted entrepreneurs, there have been triumphs due to the entrepreneurial spirit, ingenuity, and resilient nature of entrepreneurs across America. However, entrepreneurs have consistently identified a preponderance of regulatory burdens, limited access to capital, excessive taxation, and a state of general confusion understanding the myriad of policies and mandates coming from the federal (and often compounded by their states’) government. This hearing represents an opportunity to hear from entrepreneurs about both factors that promote entrepreneurship across the United States as well as the obstacles that hinder their success.

²⁴ BRINK LINDSEY, EWING MARION KAUFFMAN FOUNDATION, FRONTIER ECONOMICS: WHY ENTREPRENEURIAL CAPITALISM IS NEEDED NOW MORE THAN EVER 5 (Apr. 2011), *available at* http://www.kauffman.org/uploadedfiles/frontier_economics_4_06.pdf.

²⁵ *Id.*

²⁶ *Id.*

²⁷ *Id.*

²⁸ https://www.bea.gov/newsreleases/regional/gdp_state/gsp_newsrelease.htm.