Why Track New Firm Creation?

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New Firms

• System Consequences
  – Major source of new jobs
  – Major source of productivity gains
  – Major role in innovation, adaptation
  – Associated with economic growth
  – Related to shifts in economic structure

• Individual Consequences
  – Major career option for many
  – Route for status enhancement
  – Uneven distribution of costs and benefits of entrepreneurial activity
Productivity Assessments

- Productivity defined as labor expenditures as proportion of all costs
- Use longitudinal studies of a panel of firms
- Control for technology by focusing on specific sectors
- Assess impact on sector productivity from:
  - Continuing firms
  - Net entry [new firms less exiting firms]

Sources of Sector Productivity (10 year period)

<table>
<thead>
<tr>
<th>Source</th>
<th>Relative Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retail, All</td>
<td>5.0%</td>
</tr>
<tr>
<td>Department Stores</td>
<td>40.0%</td>
</tr>
<tr>
<td>General Merchandise</td>
<td>-40.0%</td>
</tr>
<tr>
<td>Manufacturing, All</td>
<td>70.0%</td>
</tr>
<tr>
<td>Net entry</td>
<td>95.0%</td>
</tr>
<tr>
<td>Continuing Estab</td>
<td>60.0%</td>
</tr>
<tr>
<td>Net Entry</td>
<td>140.0%</td>
</tr>
</tbody>
</table>

Net entry = new entrants less exits.
Association with Growth

- Consider gross measures of growth
  - Change in GDP
  - Net job gains
- Results indicate strong association
- Causal mechanism not clear
  - Entrepreneurship may be significant as a catalyst

TEA Index Rates and National Economic Growth: 1 Year Lag [Pooled data]

<table>
<thead>
<tr>
<th>TEA Index Rates (TEA=Active in Start-up Process or New Firm Management)</th>
</tr>
</thead>
<tbody>
<tr>
<td>5.000</td>
</tr>
<tr>
<td>10.000</td>
</tr>
<tr>
<td>15.000</td>
</tr>
<tr>
<td>20.000</td>
</tr>
<tr>
<td>25.000</td>
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<tr>
<td>30.000</td>
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</table>

<table>
<thead>
<tr>
<th>Percent Growth in GDP, Local Currency, Constant Prices</th>
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<tbody>
<tr>
<td>-4.00</td>
</tr>
<tr>
<td>-2.00</td>
</tr>
<tr>
<td>0.00</td>
</tr>
<tr>
<td>2.00</td>
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<tr>
<td>4.00</td>
</tr>
<tr>
<td>6.00</td>
</tr>
<tr>
<td>8.00</td>
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<tr>
<td>10.00</td>
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</tbody>
</table>

R = 0.45
New Firm Births and Job Changes: Two year lag

US Labor Market Areas:
Data Pooled for 6 Two-year periods. [n=2,292]

New Firm Births and Job Growth: Two Year Lag

394 US Labor Market Areas
New Firm = New Listing in National Social Security Register

Annual Average Job Increase: 2001-2003

New Firm Births/100 Firm

1990-2001: New Firms/1,000 Lab For

Percent change in Jobs

New Firm= New Listing in Credit Rating File

R = 0.30

R = 0.39

Innovation and Firm Size

• Innovations identified from technical and scientific literature [n=8,074]
  – Had to be a product in the marketplace
  – None created a new market category
  – Three levels of “impact” on markets
• Source of innovation then tracked down
  – Size based on total firm
• Source organization classified as small or large, more or less than 500 employees
• Not ideal, but suggestive
• Compare scope of small, large firms in economy

Innovation in the Market by Firm Size: US 1982

Percentage of Total

- First of type
- Significant Improvement
- Modest Improvement
- All Innovations in market
- Proportion of firms
- Proportion of employment

Small Firms [<500] Large Firms [<500]
System characteristics

- In advanced economies
  - Number of firms continues to grow
  - Size of typical firms continue to shrink
  - Specialization of firms increases
- Interdependence among elements seems to be increasing
- Interdependence across national boundaries is also increasing

Global Scope of Activity
[40 countries – 2003; 62% of world population]

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<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Total population: 40 Countries</td>
<td>3,970,000,000</td>
</tr>
<tr>
<td>Total working age: 18-64 yrs old</td>
<td>2,443,000,000</td>
</tr>
<tr>
<td>Nascent Entrepreneurs</td>
<td>297,000,000</td>
</tr>
<tr>
<td>Total start-up, new firms</td>
<td>192,000,000</td>
</tr>
</tbody>
</table>
Status Enhancement

- New Firm Creation often bypasses major societal mechanisms for controlling access to education, prestige positions
- Markets often blind to class and ethnic characteristics
- Higher rates of participation among immigrants
  - Frequently very visible in retail, services
  - Usually a small proportion of total

Costs and Benefits

- Major benefits
  - Accrue to those with successful new firms
  - New firms provide social benefits
    - Jobs, new products, new technology etc.
- Major costs
  - Born by those (and their families)
    - The 60% that do not complete start-up with new firm
    - The new firms that never pays back the start-up investment
- More complete understanding of the process may
  - Reduce the social and individual costs
  - Improve the benefit/cost ratio for society
Conclude

- A lot of progress has been made
  - Defining the critical issues
  - Methodological and data collection
    procedures to promote harmonized data sets
- Major opportunities are present for
  developing a complete, empirically based,
  policy relevant understanding of
  entrepreneurial phenomena

References

- Sources of Jobs
- Entry and productivity
- Innovation
- Economic Growth
- Shifts in Economic Structure
- Global Scope of Individual Participation