

MODULE 1: THE ROLE OF SMALL BUSINESS

Teaching Notes:

Module 1 Objectives:

- Understand perceptions and definitions of entrepreneurship.
 - Understand the definitions of "small business" and why this is important.
 - Identify major characteristics of an entrepreneur.
 - Learn about the role small business plays in the U.S.
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Understand perceptions and definitions of entrepreneurship.

- **What is an entrepreneur?**
 - **Dictionary** - "The word entrepreneur originates from the French word, *entreprendre*, which means "to undertake." In a business context, it means to start a business. The Merriam-Webster Dictionary presents the definition of an entrepreneur as one who organizes, manages, and assumes the risks of a business or enterprise." (Source: www.quickMBA.com).
 - **Perception** - "The concept of entrepreneurship has a wide range of meanings. On the one extreme an entrepreneur is a person of very high aptitude who pioneers change, possessing change characteristics found in only a very small fraction of the population. On the other extreme of definition, anyone who wants to work for himself or herself is considered to be an entrepreneur." (Source: www.quickMBA.com).

➤ **EXERCISE:** 1-1

Understand the definitions of "small business" and why this is important.

- **Intro** - We all have our own ideas of what constitutes a "small business". You might envision a husband and wife team running a bakery in your town. You might also envision a large information technology company with 75 employees and millions of dollars in sales. In fact, both of these examples could be small businesses.

➤ **EXERCISE:** 1-2

- **HOMEWORK 1-2:** On the SBA Website, look up the size classification of the business the shared in the class exercise. Report back in next class. Link to follow: <http://www.sba.gov/size/indexableofsize.html>

- **Business size** - Business size can be assessed in a number of ways, including number of employees and revenues.
 - **The Small Business Administration** – A federally-funded government agency providing loans and assistance to small businesses.
 - **The Small Business Act and NAICS** - The SBA adheres to The Small Business Act which states that a small business concern is "one that is independently owned and operated and which is not dominant in its field of operation." The law also states that in determining what constitutes a small business, the definition will vary from industry to industry to reflect industry differences accurately. The SBA produces a [table](#) of size standards, matched to North American Industry Classification System (NAICS) industries, to guide the definition of a small business.
 - What does this mean?
 - Independently owned and operated – For example, the company could not be a part of Coca Cola, it must be independent.
 - Not dominant in its field of operation – Google, for instance, is dominant in its field of operation.
 - The definition will vary from industry to industry – This is where the size chart is relevant. (See overhead 1-B).
 - **Rule of thumb** - On average, the SBA defines most small businesses as having 500 or fewer employees, and revenues not exceeding \$6 to \$8 million.
 - This can vary widely depending on the industry.
 - A business could be as large as \$30 million, or have as many as 1000 employees, and still be considered a small business according to the SBA.
 - Of all businesses in the US with employees, four of five businesses have fewer than 20 people working in them. (Source: Dennis, William J., "NFIB Small Business Policy Guide". November, 2000).
 - **Additional important notes about business size-real life example:**
 - Federal agencies must use the SBA's size standards when awarding contracts to small businesses.
 - Many private companies and states also use the SBA's size standards when awarding contracts to small businesses, although, some develop their own size standards.
 - Financing institutions, including the SBA itself, often make "small business loans" to businesses that meet the criteria for a small business.
 - Takeaways:
 - A small business's status as an actual SBA-defined (or otherwise defined) "small business" can be important to a potential client.
 - The small business owner must be aware of this and educate herself or himself on the size standards the client uses.
- **EXERCISE:** 1-2a
- **Overall: Did you realize that small business is everywhere?:**
 - From your hairdresser to a high tech companies,

- From your school to your doctor's office,
 - From the farmer who grows the food you eat to the manufacturer that made the furniture in your living room.
- **HOMEWORK 1-2a:** Continuing exercise 1-2a, on your way home today pick three businesses you see, write them down, and look them up on the SBA size chart. (<http://www.sba.gov/size/index.html>)

Identify major characteristics of an entrepreneur.

- **Intro** – Comparison of perceptions of entrepreneurial traits:
 - Many texts focus on a broad range of skills needed to get started and remain successful.
 - Entrepreneurs, when interviewed, will often focus on the defining traits which have made them a success.
- **Text traits** - *Essentials of Entrepreneurship and Small Business Management*, by Thomas W. Zimmerer and Normal M. Scarborough is one of the nation's top text books for entrepreneurship. Here is how the text defines key traits of an entrepreneur:
 - **Desire for responsibility** – Entrepreneurs feel responsible for the endeavors they start. They want to control the goals that are developed, and the resources deployed to achieve that goal.
 - **Preference for moderate risk** – Entrepreneurs are calculated risk takers.
 - **Confidence in their ability to succeed** – Entrepreneurs must be optimistic about their chance for success. NFIB found that business owners rated the success of their companies quite high: An average of 7.3 on a scale of 1 (a total failure) and 10 (an extreme success). [National Small Business Poll: "Success, Satisfaction, and Growth". National Federation of Independent Businesses (Washington, DC), 2002, p2.]
 - **Desire for immediate feedback** – Entrepreneurs are continually looking for feedback on their ideas and their business.
 - **High level of energy** – Entrepreneurs are more energetic than the average person, they have to be.
 - **Future orientation** – Entrepreneurs are able to visualize opportunities in the future. "They are less concerned about what they did yesterday and more concerned about what they might do tomorrow."
 - **Skill at organizing** – Building a company "from scratch" is a challenge. Entrepreneurs know how to assemble the right team and resources to accomplish their goal.
 - **Value of achievement over money** – It is a misconception that entrepreneurs care only about money. Money is just one measure of achievement. Doing what seems impossible is the larger value system for the entrepreneur.

Other characteristics include:

- **High degree of commitment** – There are many barriers to overcome in starting and running a business.
- **Tolerance for ambiguity** – There is no rule book in starting and running a business. Entrepreneurs have to be able to tolerate this ambiguity.
- **Flexibility** – Adapting to changing demands is a key entrepreneurial trait.

Source: Zimmerer, Thomas W. & Scarborough, Norman M. *Essentials of Entrepreneurship and Small Business Management*. Prentice Hall, 2005.

• **Entrepreneurial traits - What entrepreneurs say:**

- **Tenacity and drive** – Entrepreneurs often describe many tough times and failures. Having the tenacity to muscle through these times is a critical trait. The will to succeed must prevail for the successful entrepreneur.
- **Opportunity “vision”** – The ability to see and seize an opportunity, not just when starting the business, but throughout the business's life.
- **Passion** – An entrepreneur who has passion for what they do has a trickle down effect in the business. It energizes the entrepreneur, the clients, and the staff.
- **Relationships** – Whether a mentor, client, business partner or other relationship, many entrepreneurs have benefited from maintaining good personal relationships. These relationships have played a role in their business later in life.
- **Judgment** – Willingness to enforce good judgment and to make decisions including: Financing, hiring and firing, or the “next phase” of growth. Having good judgment helps entrepreneurs make the right decision time and time again.

Source: Frey, Katherine Korman. “T-SET: The Successful Entrepreneurial Traits”. Whitepaper, 2004.

➤ **EXERCISE 1-3:** Entrepreneurial traits survey & discussion.

- **About what are you passionate?** In thinking about a business to work in, it's good to start with something you like.

➤ **EXERCISE 1-3a:** About what are you passionate? Use exercise 1-3a to engage students in thinking about their hobbies and interest areas...In other words, things about which they're passionate. Students will keep this exercise for use in Module 2.

Small business in the American economy

- **YESTERDAY**

- **One product at a time** - "Until the early 1800s, most goods were produced on at a time by workers in their cottages or in small artisan studios. Much of the US economy was based on agriculture." (Hatten, Timothy, *Small Business Management*).
- **The Industrial Revolution & Economies of Scale** - What changed it all? The Industrial Revolution.
 - Example: Eli Whitney's cotton gin.
 - Example: Samuel Slater's textile machine.
 - These advancements made it possible to produce more than one item at a time.
 - Factories were created to house the people, materials, and machineries required to make the goods.
 - Economies of scale developed - The more the factories produced, the less each item cost.
 - Example: Henry Ford developed an assembly line system for manufacturing cars.
 - Example: Andrew Carnegie founded US Steel and produced steel in mass quantities.
- "Although these individuals had begun as entrepreneurs, their companies eventually came to dominate their industry."

Source: Hatten, Timothy S. *Small Business Management: Entrepreneurship & Beyond*. Houghton Mifflin, 2003.

- **TODAY:**

- **Current climate for business growth** - Just like the Industrial Revolution, growth and success for these businesses is realized through greater efficiencies and greater innovations.
 - Example: Wal-Mart's operational efficiencies which drove many competitors out of business.
 - Example: The "Palm Pilot" which revolutionized the way people kept their calendars.
- **Small business's ability to compete** - Small businesses have thrown their hats in the ring and, in many cases, are able to compete with larger firms due to advances in technology:
 - "The capital advantage big businesses sometimes have is being eliminated. The technology is helping smaller companies beat up the big guys." Ted Stolberg, venture capitalist. (Source: Hatten, Timothy. *Small Business Management*, p.11).

- **Universities and entrepreneurship** - Universities recognize the importance of supporting entrepreneurship. "In 1971 only 16 schools in the US offered courses in entrepreneurship. By 1993, that number had grown to 370." (Hatten, Timothy, *Small Business Management*, p.10). As of 2003, approximately 1,600 universities offered 2,200 entrepreneurship or new venture courses. (Katz, J.A., "The Chronology and Intellectual Trajectory of American Entrepreneurship". *Journal of Business Venturing*, v.18(2): 283-300.)
- **Today - Key Facts 1: Number of small businesses**
 - **In 2002, there were approximately 22.9 million small businesses in the United States, according to Office of Advocacy estimates.** The Internal Revenue Service (IRS) estimates there were 26.4 million business tax returns in 2002; (However, this number may overestimate the number of firms, as one business can operate more than one taxable entity). (Source: Small Business Administration).
- **Today - Key Facts 2: Role in Economy** - Did you know small businesses:
 - Represent more than 99.7 percent of employers.
 - Employ more than half of all private sector employees.
 - Additional Note: Small business is especially important for its contributions to the jobs in the US. While large companies create wild swings in the job force through expansion or layoffs, small business is a stabilizing force. (National Federation of Independent Businesses, Policy Guide).
 - Create more than 50 percent of nonfarm private gross domestic product (GDP).
 - Additional Note: This means that, excluding agriculture, small business produces half of the gross domestic product, or the total value of goods and services produced by a nation.
 - Produce 13 to 14 times more patents per employee than large patenting firms. These patents are twice as likely as large firm patents to be among the one percent most cited.
 - Are employers of 39 percent of high tech workers (such as scientists, engineers, and computer workers).
 - Additional Note: The National Federation of Independent Business tells us that in no other country has small business played more important a role in the innovative process.
 - Made up 97 percent of all identified exporters and produced 29 percent of the known export value in FY 2001.
 - Additional note: This means almost one third of all exports are produced by small business.

Primary bullet point sources: U.S. Bureau of the Census; Advocacy-funded research by Joel Popkin and Company (Research Summary #211); Federal Procurement Data System; Advocacy-funded research by CHI Research, Inc. (Research Summary #225); Bureau of Labor Statistics, Current Population Survey; U.S. Department of Commerce, International Trade Administration.

- **Today - Key Facts 3: Industry and type breakdowns.**
 - **Sole proprietorships** (about which the students will learn more in later modules) are the most popular type of small business comprising approximately 17.5 million of the approximately 22 to 26 million small businesses in the US.
 - Of these 17.5 million sole proprietorships, the majority are service based businesses (see overhead 1-D, figure 1):
 - **Homebased businesses** make up approximately 53% of small businesses in the US (Small Business Administration, "State of Small Business", p.2, 2004).
 - Of these, 52% are in service industries
 - 16% are in construction
 - 14% are in retail trade
 - All other types of businesses comprise no more than 6% of the amount.
- **Today - Key Facts 4: Women and Minority-Owned Small Businesses** – Women and minority owned businesses are growing at astounding rates. "There has been significant growth in women's entrepreneurship among every major racial and ethnic group," said Myra M. Hart, Professor, Harvard Business School and Chair, Center for Women's Business Research. (Source: Center for Women's Business Research, "Businesses Owned by Women of Color Growing Faster than the Overall Economy". 2004.).
 - Firms owned by women of color are growing at six times the rate of all U.S. firms, according to estimates released by the Center for Women's Business Research and underwritten by Bank of America. Between 1997 and 2004, the number of privately-held firms that are 51% or more owned by women of color grew by 54.6%, while all privately-held firms in the United States grew by 9.0%.
 - As of 2004, there are an estimated 10.6 million privately-held, 50% or more women-owned firms in the U.S., accounting for nearly half (47.7%) of all privately-held firms in the country. Between 1997 and 2004, the growth in the number of 50% or more women-owned firms is nearly twice the rate of all firms (17.4% vs. 9.0%),
 - Resource: Center for Women's Business Research
<http://www.nfwbo.org/>
- **Final Thoughts: Small Business in the U.S. – a culture of entrepreneurship.** Why has such an important small business sector developed in the US?
 - **Opportunity:** Most American small business owners start businesses based on the opportunity it provides them personally, professionally, or a combination of both (National Federation of Independent Business, Policy Guide).
 - "Small businesses enable millions of people, including women, minorities, and immigrants, to access the American Dream. (Small Business Administration, 1998)."

- **Culture:** Culturally, Americans readily organize around a cause, be it community, commercial, or otherwise: "Americans of all ages, all conditions, and all dispositions, constantly form associations." (Alexis De Tocqueville, *Democracy in America*.)
 - In no other country has small business played more important a role in the innovative process. This is thought to be due, in part, to the American culture's ability to tolerate failure as a logical outcome of trying something new. (The National Federation of Independent Business).
- **Future Orientation:** "U.S. economy is a dynamic, organic entity always in the process of 'becoming' rather than an established one that has already arrived. It is about prospects for the future, not about the inheritance of the past. (Kuratko, Donald. "Entrepreneurship Education: Emerging Trends and Trends for the 21st Century". 2003.)
- **Public Support:** The US enjoys a culture that strongly supports small business and entrepreneurial activity. Those favorable opinions have a significant influence on the ultimate success of small firms. ("The Public Reviews Small Business," conducted by the NFIB Research Foundation.)

Thinking ahead: In the next module we will begin to explore some of the first steps future entrepreneurs should consider in starting a small business. One critical factor is: Should I start a small business? I may have an idea or passion I would like to pursue, but, do I have the correct motivations? According the National Federation of Independent Business:

- Approximately two-thirds of starting entrepreneurs expect their venture to be full time. They intend to grow the business in the future or for the business to provide a good living for them.
- Approximately one-third of starting entrepreneurs intend their venture to be part time.
- About 82.5% of entrepreneurs seek credit of some type, be it bank financing, credit cards, or financing from friends and family. (Small Business Administration).

HOMEWORK: Have students refer to NFIB's 2003 Small-Business Policy Guide (Chapter 4, Exhibit 3.4: link <http://www.nfib.com/object/2753115.html>) for some additional motivations for starting a business.

QUIZ: Administer multiple choice quiz on Module 1.