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Editor: Jock A. Finlayson

SMALL BUSINESS GROWTH

The role of small businesses necessarily features prominently in any discussion of the structure and performance of British Columbia’s economy. It is no exaggeration to say that an orientation toward small businesses is one of the defining characteristics of the province’s economy.

The most recent Small Business Profile¹, an annual publication co-produced by BC Stats and Western Economic Diversification Canada, provides a wealth of useful information on the number and distribution of businesses across the province. In developing the report, the government agencies classify as “small businesses” all enterprises with fewer than 50 paid employees, plus the numerous businesses operated by self-employed individuals with no paid help. “Large businesses” are those with 50 or more paid workers.

Table 1 summarizes some of the key findings of the latest Small Business Profile report. In 2008 there were 391,300 businesses in British Columbia, of which 98% were “small.” Many of these small firms consist of self-employed individuals and have no paid workers. In fact, more than half of all businesses in BC fall into this category. There are only 7,000 enterprises in the province that directly employ 50 or more people.

Chart 1 shows the distribution of employment in the business sector as of 2008. In total, 1.89 million British Columbians earned their livelihood in the private sector. “Large” enterprises accounted for 44% of private sector jobs, while “small” businesses with paid workers were responsible for one-third. Remarkably, almost one-quarter of private sector jobs were supplied by self-employed individuals running their own businesses without paid help. Some of these are self-employed professionals – e.g., lawyers, accountants, physicians, dentists, independent financial planners – while many others operate

| | Number of Businesses | Per cent of Total |
|---|-------------------------|----------------------|
| Total small businesses | 384,300 | 98% |
| Self-employed without paid help* | 216,300 | 55% |
| Businesses with less than 50 employees | 168,000 | 43% |
| Total large businesses | 7,000 | 2% |
| Total all businesses | 391,300 | 100% |

* Incorporated self-employed are not included in this figure in order to avoid double-counting, since they are already included in the count of businesses with fewer than 50 employees.

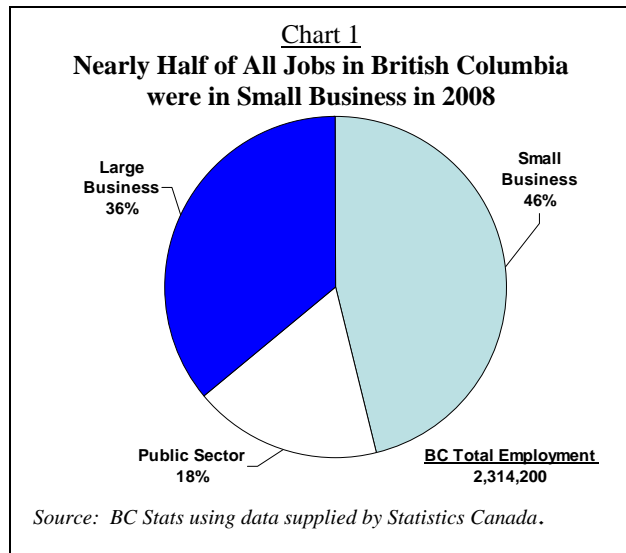
Source: BC Stats using data supplied by Statistics Canada.

¹ BC Stats and Western Economic Diversification Canada, Small Business Profile, 2009. Available from www.gov.bc.ca/sted



tiny home-based businesses in areas like home cleaning, home renovation, consulting, landscaping, hairdressing, etc.

Among firms with paid workers, “large” companies actually employ significantly more British Columbians (834,700) than do their smaller counterparts (629,800). The proportion of total employment in the “small business” sector has been essentially stable for the past decade.² Thus, the claim that small businesses are responsible for virtually all job creation is incorrect. Particularly in a growing economy, all size categories of businesses tend to be adding jobs.



Importance of Fast-Growing Firms

In the United States, the pioneering work of Birch in the 1980s underscored the vital contribution of the fastest-growing firms – “gazelles” was the term he used – in driving job creation.³ Recent American research strongly reinforces this finding. A study from the Kauffman Foundation estimates that, in a typical year, the top-performing 5% of American businesses – measured by employment growth – generate two-thirds of all new jobs. And the top 1% of firms are responsible for 40% of job creation.⁴ Thus, a relative handful of companies account for a markedly disproportionate share of employment growth at an economy-wide level.

Most businesses in the top 5% and top 1% categories are fairly young – less than ten years old – and are small or medium-sized, as defined by US statistical agencies.⁵ For example, the average US firm in the top 1% group added 88 new jobs per year. The picture that emerges from this research is that, over a period of several years, a few thousand US companies grow from small to reach very substantial size, employing 2,000-10,000 people each. As the Kauffman Foundation study observes: “These super high-growth [companies] become *scale firms*, the next generation of iconic companies.”⁶

Turning to Canada, a recent paper done for Industry Canada explored the issue of fast-growing entrepreneurial firms. The authors determined that between 4% and 8% of all

² Ibid., p. 9.

³ D. Birch, “Change, Innovation and Job Generation,” *Journal of Labor Research*, volume 10, number 1 (1989), pp. 33-39.

⁴ Dane Stangler, *High Growth Firms and the Future of the American Economy*, Kauffman Foundation Research Series: Firm Formation and Economic Growth (March 2010). Available from: www.kauffman.org

⁵ In the US, small businesses are generally classified as those with fewer than 250 employees; medium-sized as those with 250-500 employees; and large firms as those with more than 500 paid workers.

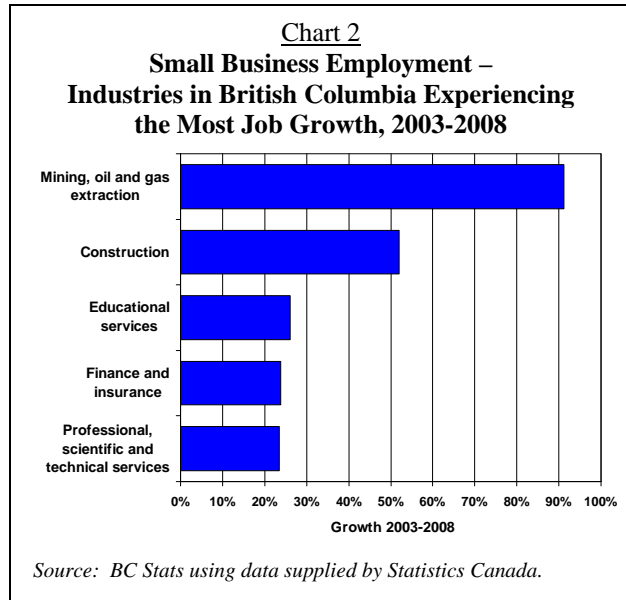
⁶ Stangler, *High Growth Firms and the Future of the American Economy*, op. cit., p. 6; emphasis added.



Canadian businesses are “high growth” as measured by their increases in employment or sales, respectively. (Specifically, such firms had to be expanding jobs or sales by at least 20% a year over a three-year period to be counted as high-growth.) In the same year, only 0.5%-1.0% of Canadian firms grew fast enough to qualify as “gazelles.”⁷ The authors conclude that Canada compares favourably with several other advanced countries on indicators of entrepreneurial activity.

Unfortunately, there is little data on individual provinces that is comparable to the information in the aforementioned Industry Canada study. The annual Small Business Profile produced by BC Stats and Western Economic Diversification Canada does track growth in the number of businesses by industry and by region, but the data are quite limited and there is no attempt to isolate the economic contributions of the subset of very rapidly growing firms.

In 2008, the sectors that saw the biggest jumps in the absolute numbers of active firms in the province were construction and business services. From 2003 to 2008, construction was also the largest provider of new “small business” jobs (30,360), followed by professional, scientific and technical services (11,800). However, in percentage terms, mining and oil and gas extraction posted the strongest job growth, followed by construction and educational services (see Chart 2).



Understanding the Differences

The small business world can be divided into two types of firms: a huge number of “main street” businesses that don’t grow much if at all but collectively employ lots of people and provide a wide array of needed goods and services; and a much smaller number of “gazelles” which expand rapidly and are key sources of job creation, increased productivity, and innovation. “Main street” businesses are found in many sectors of our economy but are particularly ubiquitous in industries like retail, foodservices, dry-cleaning, car repair, construction, and personal and business services. They are a critical part of the business community but generally don’t contribute much to net job creation.⁸ There is a high level of “churn” in these sectors, as some existing firms disappear and new ones are formed each year.

⁷ Industry Canada, The State of Entrepreneurship in Canada (February 2010). Report compiled for Industry Canada by Eileen Fisher and Rebecca Reuber. Available from: www.ic.gc.ca/research

⁸ That is, while some small firms in these sectors create jobs, others eliminate jobs as they shrink or disappear.



Rapid-growth firms follow a different path. The entrepreneurs who form these companies are crucial to their ongoing expansion. Importantly, fast-growing “gazelles” are found in many industries (not just high-technology, software, entertainment, etc). Table 2 reports on the ratio of the share of net jobs created by fast-growing Canadian firms in various industries to these industries’ share of all strong-growth firms in the national economy. The data highlight the fact that “gazelles” exist across a wide spectrum of industries. Of interest, the highest ratio was in transportation equipment industries, at 5.4. This means the share of jobs created by high-growth firms in transportation equipment industries was 5.4 times greater than these industries’ share of all fast-growing Canadian firms.⁹ Table 2 displays the ratios for the top 20 industries as ranked by this particular measure.

An interesting question is whether fast-growing “gazelles” develop essentially on a random or accidental basis, depending mainly on the distribution of entrepreneurial talent and ambition, or whether they are more likely to emerge in particular regions or at times of disruptive technical change. There are conflicting views on this among researchers. The good news is that policy-makers can help to establish conditions in which gazelles are more likely to flourish. Making it simple to start a new business is one example – and this happens to be an area where Canada scores well according to international benchmarks.¹⁰ Ensuring that capital is available to fund start-ups as well as promising growth-oriented business ventures is important. This includes not only venture capital but also other sources of business financing (mezzanine funding, bank loans, angel networks, etc.). Finally, establishing a tax structure that rewards entrepreneurial success, attracts equity investment, and encourages successful firms to grow is also critical.

Table 2
Ratio of the Share of Jobs Created to the Share of Hyper and Strong Growth Firms within the Industry, Canada, 1993-2003

| <u>Rank</u> | <u>Industry</u> | <u>Ratio*</u> |
|-------------|--|---------------|
| 1 | Transportation Equipment Industries | 5.4 |
| 2 | Other Service Industries | 4.7 |
| 3 | Rubber Products Industries | 3.7 |
| 4 | Shoe, Fabric and Yarn Stores | 3.3 |
| 5 | Beverage Products Industry | 2.8 |
| 6 | Food Industries | 2.8 |
| 7 | Amusement and Recreational Service Industries | 2.5 |
| 8 | Metal, Hardware, Plumbing, Heating and Building Supplies | 2.2 |
| 9 | Furniture and Fixture Industries | 2.2 |
| 10 | Oil and Gas Industry | 2.1 |
| 11 | Non-Metallic Mineral Products | 2.1 |
| 12 | Publishing and Printing Industries | 1.9 |
| 13 | Mineral Extraction Services | 1.7 |
| 14 | Machinery Industry | 1.7 |
| 15 | Clothing Industry | 1.7 |
| 16 | Wood Industries | 1.6 |
| 17 | Department Stores and General Merchandise Stores | 1.3 |
| 18 | Fabricated Metal Products | 1.3 |
| 19 | Accommodation Service Industry | 1.3 |
| 20 | Machinery Equipment and Supplies Wholesale | 1.3 |

* Share of Jobs Created to Share of Firms
Source: Industry Canada.

⁹ Industry Canada, *Profile of Growth Firms: A Summary of Industry Canada Research* (March 2008).

¹⁰ World Bank, *Doing Business 2010: Reforming Through Difficult Times* (2010). Available at www.doingbusiness.org