



Bridging the Gap: Overcoming Minority Small Business Performance Disparities



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Moderator: Welcome to the Federal Reserve Bank of Atlanta's Small Business podcast series. I'm Todd Greene with the Federal Reserve Bank of Atlanta. Today we're talking with Dr. Robert Fairlie, professor in applied economics and finance with the University of California, Santa Cruz.

In the 2008 book, *Race and Entrepreneurial Success: Black-, Asian-, and White-Owned Businesses in the United States*, Dr. Fairlie and his co-author Alicia Robb explore the trends and dynamics of minority small business and the determinants of their success. The book notes the important contribution that minority businesses make to the U.S. economy overall, creating nearly 5 million jobs. The foreclosure crisis and economic recession have exerted significant pressure on all small businesses and have prompted lively debate about the best responses to support small and young businesses and their job creation capacities. In this podcast, we will explore how minority-owned small businesses have fared, and policy options to support them.

Dr. Robert Fairlie joined the economics faculty of UC Santa Cruz in 1994. His research includes entrepreneurship, minority business ownership and outcomes, the digital divide, racial patterns in unemployment and job displacement, welfare reform, and the U.S. educational system.

Dr. Fairlie, thank you for joining me today.

Dr. Robert Fairlie: Yes, I'm glad to be here.

Moderator: Your paper, titled "The Great Recession and Entrepreneurship," addresses the effects of the recession on entrepreneurship, and whether the tightened credit market is hampering entrepreneurship or pushing more people to become entrepreneurs out of necessity. Please tell us the results of your research and the trends you have observed.

Fairlie: So, we hear a lot about the recession that we are currently in; it's even called The Great Recession because of the large hit that it's taken on workers. And so what I was interested in in this paper is trying figure out what effect it's had on business creation. So the idea being, if a lot of people are losing their jobs, what are their opportunities? Are they going to start businesses, or remain unemployed?

And so, one of the things that I wanted to look at was the effects of local labor market conditions on business creation. We certainly know that the recession has created a lot of business closures, business foreclosures, and other aspects of businesses going out of business, but we don't know that much about business creation. And so, the idea is, if you live in an area, or during a time when local labor market conditions are bad, in terms of high unemployment rates, does that create individuals to start businesses? And so, what I find is that it does have a large effect. I find that if you increase the unemployment rate in a local labor market by 5 percent, that increases business creation by roughly 15 percent.

I also examined the effects of the housing market on entrepreneurship. In particular, I looked at homeownership rates that have been declining and home values that have also been declining and what effects they've had on entrepreneurship. Both of those have negative effects on entrepreneurship, but much smaller than what we find for local labor market conditions. So, in the end, the positive effect of rising unemployment in The Great Recession outweighs the negative effects of the declining housing market and declining home ownership in terms of increasing entrepreneurship.

Moderator: Your 2008 book, *Race and Entrepreneurial Success: Black-, Asian-, and White-Owned Businesses in the United States*, seeks to answer the question, "Why do some racial groups succeed in business while others struggle?" Based on your research, what are the determinants of business success and why has business performance differed between racial groups, historically and at the present time?

Fairlie: So in my 2008 book with MIT Press, one of the things that I was trying to figure out is, what are the determinants of business success? Specifically among smaller businesses that are not kind of large corporations. And one of the factors that we found to be the most important was access to financial capital. Another factor that was extremely important was human capital, so in terms of how educated the business owner is. And then, finally, kind of a new finding from the literature was whether or not you had an extensive family business experience. So, in particular, if you worked in your parents' business, that had a big effect on whether or not your ultimate business would be successful.

Now, if we kind of turn to the issue about minority groups, we wanted to focus on African Americans and Asian Americans. African Americans, we found in our data, had the least successful firms on average of all large…ethnic and racial groups, and Asian Americans had the most successful firms on average. And we looked at different outcomes such as sales, closure, profits, and employment at firms. And so we put these things together, and what we found is that African Americans were underperforming the national average partly because they had less access to financial capital, that they were less educated on average, and that, one of the new findings was that, they had less experience in family businesses. So they were much less likely to work in a family business than were white-owned firms.

Asian-American firms we found to be very successful for two reasons. One was that they had much more access to capital, in terms of their businesses at start-up, and also that they were highly educated. We found that 50 percent of Asian-owned businesses had an owner that had a college degree or higher, which was about twice the national average.

Moderator: In our current economic environment, many small businesses are experiencing challenges. Why is it important to address the particular disparities in small business performance between minorities and nonminorities?

Fairlie: Small-business ownership is extremely important for a number of different economic outcomes. One is it's very important for wealth accumulation. We find that business owners hold a disproportionate amount of wealth in the U.S. economy. It's also very important for job creation. Small businesses create the majority of new jobs out there. And also, for just overall economic development. If there's any community of [businesses] owned by a specific group, say a minority group, that is underrepresented in business ownership, that's going to have a negative impact on economic development in the long run.

Moderator: *What are some policy options, at the federal and the state level, to help close the business performance gaps that you've described?*

Fairlie: I think there are several things we can do. I'll focus on just a few of them. One is we need to improve access to capital. That is one of the most important issues facing small business owners in general, and also minority businesses in particular, in this recession. We need to figure out policies that can increase the capital that's provided through community banks or smaller banks or banks located in minority communities; that's going to be a key policy that needs to happen.

Another is that we need to provide training or entrepreneurship apprenticeship-type programs that provide experience working in small businesses, working in industry-specific types of jobs that allow individuals who don't have a family-business experience to overcome that deficit and be able to get the kind of experience that will help them create long-term businesses.

And then, finally, like in many other areas in the labor market, we need to eliminate discrimination. We still need to continually combat discrimination that occurs either through…these embedded social networks, these kind of "old boy" networks, and things like that. [For] those, we still need to work on removing those barriers.

Moderator: Dr. Fairlie, thank you for joining us today.

Fairlie: Thank you for having me.

Moderator: This concludes our podcast. We've been speaking with Dr. Robert Fairlie, Professor in Applied Economics and Finance with the University of California, Santa Cruz. For more podcasts on this topic and others, visit the Atlanta Fed's website at www.frbatlanta.org. If you have comments or questions, please email podcast@frbatlanta.org.

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