

Growth and Change: Does Enhancing Ohio's Small Businesses and Entrepreneurs Provide the Key to Growth?

Swank Program in Rural-Urban Policy and
The Exurban Change Project
Summary Report
January 2008

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Executive Summary

Local economic development efforts are often focused on “growing from within” to tap local investment and entrepreneurial capacity.¹ The good forms of dynamic and creative entrepreneurship are what policymakers try to encourage in order to increase economic growth, wages, wealth creation and innovation (among other things). Though not necessarily the same as entrepreneurship, greater numbers of small businesses and self employed are often associated with more entrepreneurship. Thus, facilitating small businesses and self employed is viewed as one way to promote its development.

To help assess Ohio's potential gains in building its small businesses and entrepreneurs, this policy brief aims to describe the state's entrepreneurial capacity by examining trends in self employment and innovation. We appraise how Ohio fares compared to its neighbors and to the nation. We also assess how different regions of the state are faring in terms of supporting self employment. Then we report on how well the state is doing in terms of supporting innovation. The brief concludes with some policy recommendations.

Report Highlights

- Entrepreneurship and self employment are important elements of Ohio's economy. Supporting entrepreneurship in the form of self employment can have positive spillovers for both the individual and the community.
- But, despite all of the attention placed on entrepreneurship, economists lack sufficient evidence on whether it supports local economic activity and/or whether it always produces high-paying jobs. It may simply be a “reaction” to bad events. For example, an individual may start their own business after losing their previous job without any clear plan for success.
- One spatial pattern in Ohio is that higher self-employment rates appear to be concentrated along the I-71 Corridor between Cleveland and Cincinnati and around Ohio's three major cities, suggesting that surrounding areas rely on their nearest city as an engine of growth.
- In 2005, farm self-employment was more concentrated in northwest and southeast Ohio, and obviously, less concentrated in metro counties.

- In 2005, about 86% of farm employment was accounted for by the self-employed farm operators. Agricultural services and mining also had large shares of self-employed workers, followed by finance, insurance, and real estate. Conversely, manufacturing had the lowest share of self-employment.

- Self employment became more important over time. Without the steady growth in self employment that has occurred since 2000, overall Ohio job growth would have been near zero during the first part of this decade.

- The typical self-employed rural worker today earns about ½ as much as the typical wage-and-salary worker (compared to 4 percent higher in 1969).

- While self employment appears to be a key factor in supporting more rural job growth, it is less clear whether it is providing the type of “good” jobs that will maintain a high quality of life.

- Ohio lags the national average in indicators associated with innovation including numbers of patents, IPOs, and the number of scientists and engineers. This does not bode well for future entrepreneurial capacity and wealth creation.

Highlights of Policy Suggestions:

State and Local Government Initiatives.

- The best way to provide a good climate for small business start ups is a strong Ohio economy. Efforts to reduce the tax burden by providing efficient local services that are not duplicated by other jurisdictions are key elements.

- Ohio governments should continuously strive to streamline regulatory processes and reporting burdens of small businesses. In the global economy, small reductions in costs can make the state’s businesses more competitive.

- State and local governments should be very cautious in providing tax incentives and grants. A tax incentive or a grant generally implies that the remaining businesses and residents have to pick up the tax burden.

- State and local governments should try to reduce some of the barriers to entrepreneurship. One potential barrier to being self employed or being a small business owner is the affordability of health insurance. Steps to reduce the costs of health insurance would mitigate this effect.

Workforce Training and Ohio’s Educational Institutions.

- Small businesses need access to good workers, implying a need for the state and local governments to provide better workforce training and education. Ohio should facilitate innovative activities by supporting strong nonprofits, world class educational establishments, and adequate research support. Recent state efforts to support research including the Third Frontier are good starts. Related efforts should tap Ohio’s natural and man-made assets to make the state attractive to creative and knowledge workers.

- Ohio’s universities should continue to find ways to take innovation to the market. Ohio’s higher educational institutions should strive to formalize and standardize their training of small business owners and potential entrepreneurs.



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Motivation for Understanding Entrepreneurship and Self Employment

It is increasingly believed that successful community and regional economic development more often than not occurs by “growing from within” – i.e., by tapping local entrepreneurial capacity (Dabson et al., 2003; Shrestha, Goetz and Rupasingha, 2007, Baumol et al., 2007).² Among the advantages of growing from within is that it is less necessary to attract *outside* investment for large facilities. Therefore, enhancing entrepreneurial capacity may be an effective approach in revitalizing lagging regions in Ohio including inner cities and smaller communities. Likewise, self employment and microenterprises may have larger “multipliers” if they are more likely to locally purchase goods and services. Together, these arguments would imply that the state should foster an environment that supports small businesses, microenterprises, and self employment in order to turn small businesses into thriving profitable enterprises that provide high-paying jobs.

Small businesses are already an important component of Ohio's economy. The state had an estimated 920 thousand small businesses in 2006 (U.S. Small Business Administration, 2007).³ In 2004, over 1.6 million Ohioans, or about 35% of the employed workforce, worked at nearly 203 thousand “employer firms” with between 1 and 99 employees (U.S. Small Business

Administration, 2007). Another 495,000 were self employed in 2006 and over 230,000 businesses were owned by women in 2002. Though not necessarily the same, greater numbers of small businesses are often associated with more entrepreneurship. Thus, facilitating small businesses is viewed as one way to promote its development. Thus, one can see why economic development officials often point to small businesses as a key component of a future prosperity agenda.

Under optimal conditions, an entrepreneurial climate helps promote the creation of jobs, wealth, new ideas (innovation), which then through multiplier effects, indirectly creates additional economic activities (Goetz, 2007; Goetz and Rupasingha, 2007; Loveridge and Nizalov, 2007; Monchuk et al., 2007). Strong entrepreneurial conditions may enhance a region's attractiveness to entice new capital investment and help retain the most talented workers. A stronger economy would then reduce the fiscal stress currently felt by Ohio's governments, allowing them to more adequately fund necessary services such as education and infrastructure. In sum, creating a climate of virtuous expectations would help reverse the state's downward economic slide that may act as a repellent to (new) external investment and to attracting/retaining a talented and creative workforce (Partridge, Clark, and

Enver, 2007). Nonetheless, despite all of the attention placed on entrepreneurship, economists lack sufficient evidence on whether it supports local economic activity and/or whether it always produces high-paying jobs.

Even accepting the notion that supporting entrepreneurship is worthwhile, the whole concept of local and regional entrepreneurial capacity is nebulous. What does it mean and when is it ‘good’? Does simply starting a business imply entrepreneurship? The data on this notion is hard to come by. There is no survey that simply asks a business whether they are entrepreneurial or whether a community is entrepreneurial. Just think, who would respond by stating that they are not “entrepreneurial”? Thus, researchers are forced to rely on proxies for entrepreneurship. Probably the most common measure uses self-employment, whereas another is the share of employees working in small (micro) businesses (Loveridge and Nizalov, 2007). We will use self employment as our preferred measure, but it should be pointed out that this measure includes all sorts of “self employed” from casual consulting behavior to individuals who direct a thriving business.

In a simple sense, the motivations for self employment originate from multiple sources.⁴ Abstracting away from casual self employment such as consulting, two positive motivations are (a) having a good business strategy such as replicating an innovation developed elsewhere and (b) having genuinely novel business ideas – i.e., the activity is a creative “choice.” Both (a) and (b) have positive spillovers for the affected individuals and the broader community. However, in communities facing economic

decline, individuals often feel compelled to start their own business as more of an act of desperation rather than as part of a well-defined plan developed in response to an opportunity. It is not clear that this latter type of start-up stimulates local economic growth and innovation (or perhaps it does so only partially). For example, Vigdor (2007) finds that evacuees from Hurricane Katrina are more likely to engage in self-employment activities than before the storm—though their general outcomes have relatively deteriorated.

In a related point, economic development practitioners regularly ask, why are some communities more “entrepreneurial” than others? For example, economic development officials in the Buckeye state often assert that our history of large manufacturers and unions have dampened the passion for entrepreneurship and innovation (though this claim is unproven).

More directly, entrepreneurship can take on other notions of “bad” and “good” forms (Baumol, 1990; Baumol et al., 2007). For example, Baumol et al. (2007) described four different types of capitalism. First they defined **State-Guided Capitalism** in which the government supports ‘capitalistic’ institutions. It is not clear whether this type of capitalism support growth in a developed economy such as the U.S. or Ohio. Second is **Oligarchic Capitalism** which is a type of capitalism where the economic resources are concentrated into a few families. Perhaps a “company” mining town could be an example. It is hard to see how this form of capitalism supports innovation and widespread economic growth. Third, **Big-Firm Capitalism** is more dominated by large firms. Though this form of capitalism can be dam-

aging if it doesn't encourage risk taking and innovation (or dampens competition), Big-Firm Capitalism may facilitate entrepreneurship if it helps promote the process of taking a good idea to market.

The fourth form—**Entrepreneurial Capitalism**—is commonly viewed as the type of innovative capitalism that society should promote as wealth creating and job producing. Though Baumol et al.'s categories seem sensible, it is very hard to assess whether a particular town or city in Ohio promotes one form of capitalism or another, or whether Ohio's state government facilitates capitalism in its varied good and bad forms. If we can't measure the specific types of capitalism, it is harder yet to assess whether government policy is effective.

With this in mind, should Ohio support entrepreneurship and self employment? It depends on the type that we have in mind. Clearly Oligarchic capitalism serves little value but its creative forms are much more worthwhile. Moreover, Ohio should also find ways to make the “reactive” or desperation forms of self employment or entrepreneurship more productive for the affected individuals as well as the broader community.

Given these caveats, we now discuss the underlying strengths and geographical patterns of self employment (entrepreneurship) in Ohio. We will present some of these trends and compare them to the performance of Ohio's Great Lake state neighbors, as well as to the country. Indeed, we find that comparisons to Ohio's Great Lake state neighbors are useful (Indiana, Michigan, Illinois, and Wisconsin). These states have also struggled with declining manufacturing and they have similar weather and topography, while experiencing similar settlement patterns and access to world markets. We then conclude with a discussion of policy priorities if Ohio is to promote entrepreneurship.

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The Geography of Entrepreneurship in Ohio

Table 1
Employment Data Sources

The primary data source that we use for total employment—including the number self employed—is the U.S. Bureau of Economic Analysis, Regional Economic Information System. In the fall of 2007 when we wrote this brief, the data was available for the 1969-2005 period (available at www.bea.gov). BEA data counts the number of jobs in a particular county (place of work). It does not count the number of employed residents. For example, if an individual has three part-time jobs located in a particular county, it is counted as three different jobs in that county regardless of the residence of the worker.

The U.S. Bureau of Economic Analysis data that we use for self employment are based on tax return data filed using Schedule C of IRS Form 1040. The IRS website reports that this information includes current-production income of sole proprietorships, partnerships, and tax-exempt cooperatives. It excludes dividends, monetary interest received by non-financial business, and rental income received by persons not primarily engaged in the real estate business. Clearly, the numbers can reflect activity ranging from very casual forms of consulting to an owner of a significant business entity. Each person who reports self-employment income is counted as one self-employed person.

The strength of BEA data is that it is very accurate because it is benchmarked to IRS tax returns, unemployment insurance data, and other sources. Another advantage is that it is annually available at the county level, which is not the case for other data sources. Generally, regional economists prefer place of work data because it shows the economic conditions for a particular location, while place of resident data may reflect job patterns elsewhere due to in- and out-commuting. However, counting the number of jobs does come at the disadvantage of not reflecting whether a particular job is only casual or for only a minimal number of hours. Yet, BEA data is probably the most widely used measure of self employment.

With the contraction of the manufacturing sector in recent decades, rural Ohioans are turning to entrepreneurial activities for their livelihood.⁵ Using data described in Table 1, we will see that trends in rural self-employment are promising, but average self-employment remuneration is relatively low and declining over time. In fact, the average relative return to self-employment in rural Ohio fell quite dramatically between 1969 and 2005.

Finally, we conclude with observations about the innovative activities such as patent generation that is necessary to support the creation of the most innovative entrepreneurial enterprises.

Figure 1 shows that between 1969 and 2005, the share of total non-farm employment that is comprised of self-employed workers increased by around 7 percentage points in metropolitan Ohio, in the metropolitan Great Lakes states (not counting Ohio), and in the

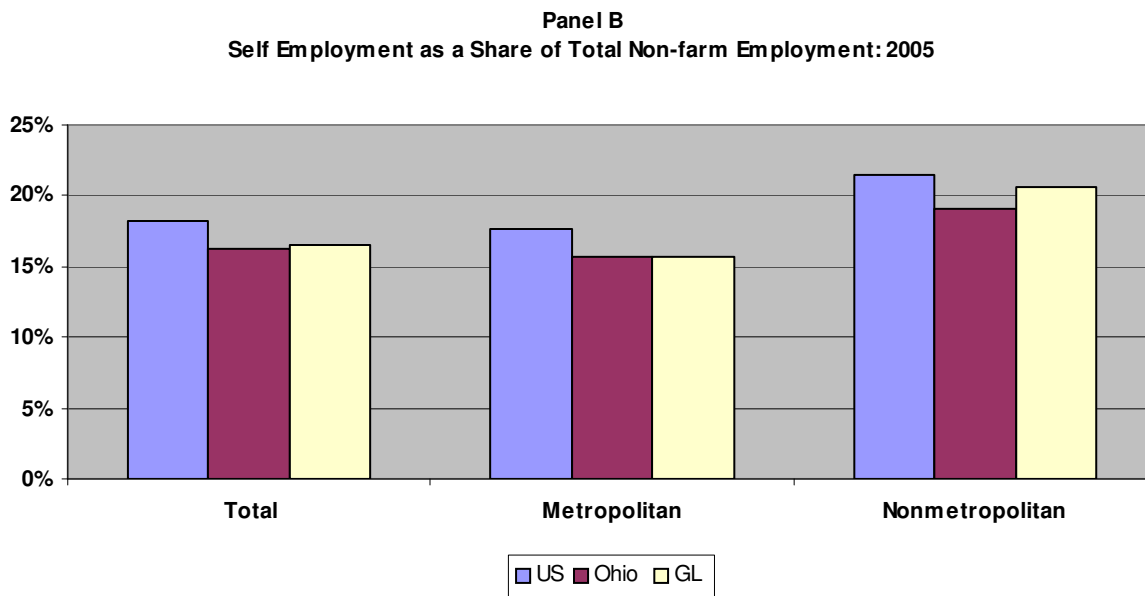
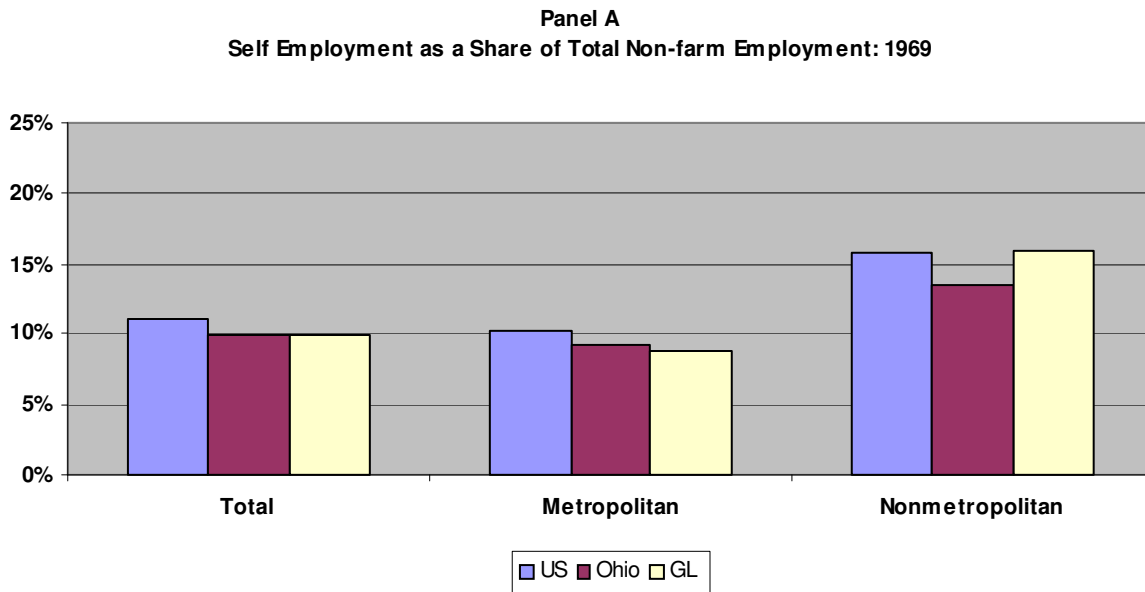


Figure 1

metropolitan United States. The corresponding increase in nonmetropolitan areas was around 5 to 6 percentage points. Generally, Ohio lags the nation and slightly lags the Great Lakes region in terms of self employment, though there is no clear pattern after 1969 except to say that self employment became more important over time.

The intensity of (non-farm) self-employment is higher in rural regions than metropolitan regions. One likely cause is simply that businesses are usually on a smaller scale in small towns than in metropolitan regions, which means a higher share of a given business's employees are (by definition) self employed

Panel A

Non-farm Self Employment as a Share of Total Employment: 2005

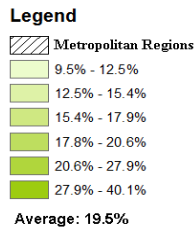
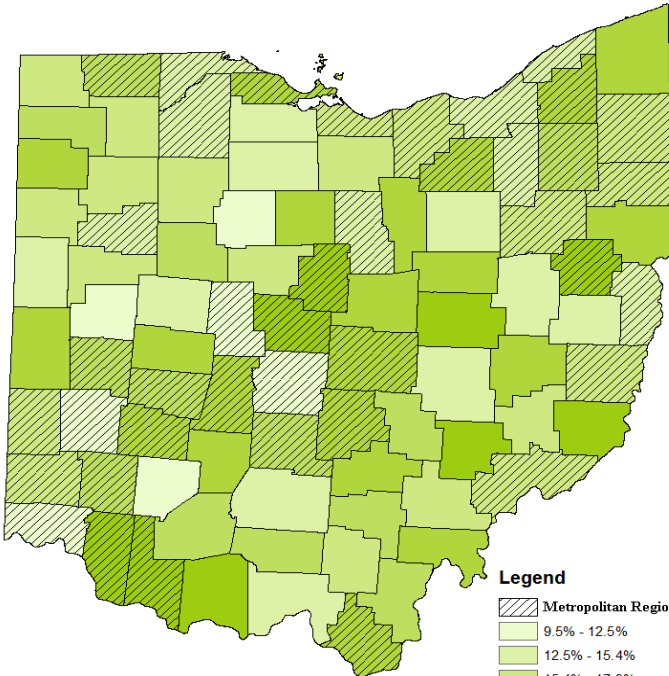
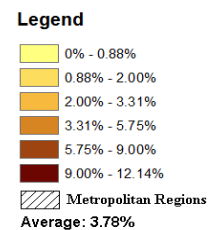
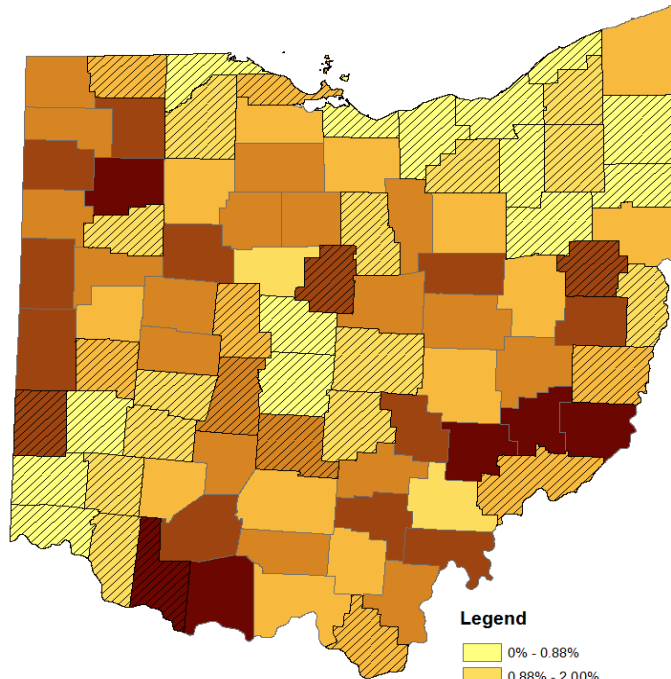


Figure 2
The Spatial Distribution of
Non-farm and Farm Self-
Employment Concentration

Panel B

Farm Self Employment as a Share of Total Employment : 2005



(or owner operator). Yet, it is less clear if rural self-employment is more or less associated with the “desperate” or “reactive” variety that is less associated with economic growth.

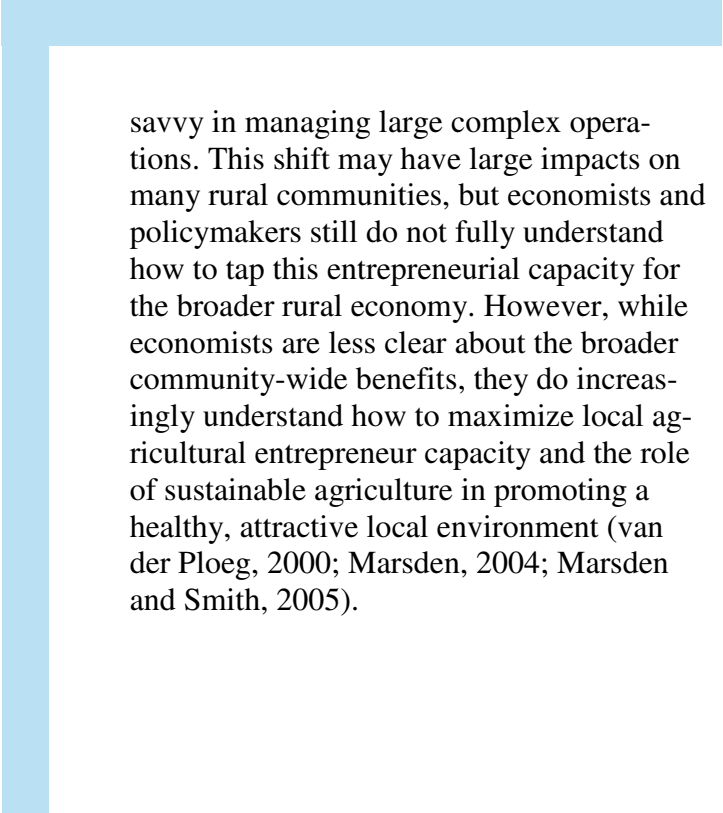
The spatial distribution of non-farm self employment across Ohio is shown in Figure 2a. It is concentrated in suburban counties surrounding the three major cities, Cleveland, Columbus, and Cincinnati in 2005, whereas, in contrast, their central counties exhibit low shares of non-farm self-employment. This pattern demonstrates that surrounding areas rely on their nearest cities as engines of growth in terms of generating entrepreneurial opportunities. For example, 13.5% of Cleveland’s (central) Cuyahoga County total employment is made up of non-farm self-employed workers, while the corresponding share in neighboring suburban Medina County is 22.6%. Similarly, Franklin County, which includes Columbus, has around 12.5% of its total employment composed of non-farm self-employed workers, while the self-employment share in neighboring Delaware County is over 30%. With Delaware county being perhaps the most vibrant county in Ohio in terms of population and job growth, it is much more likely that this type of self-employment is the entrepreneurial variety with long-term benefits. However, for Ohio policymakers, the question is whether (say) Delaware county’s high self-employment intensity causes the county to experience more economic growth or did the high growth cause the greater self employment?⁶

Another spatial pattern is that higher self-employment rates appear to be concentrated along the I-71 Corridor between Cleveland and Cincinnati. There are exceptions such as Clinton, Wayne, and Union counties, but this again raises the “chicken-egg” question of whether the self employment is causing the

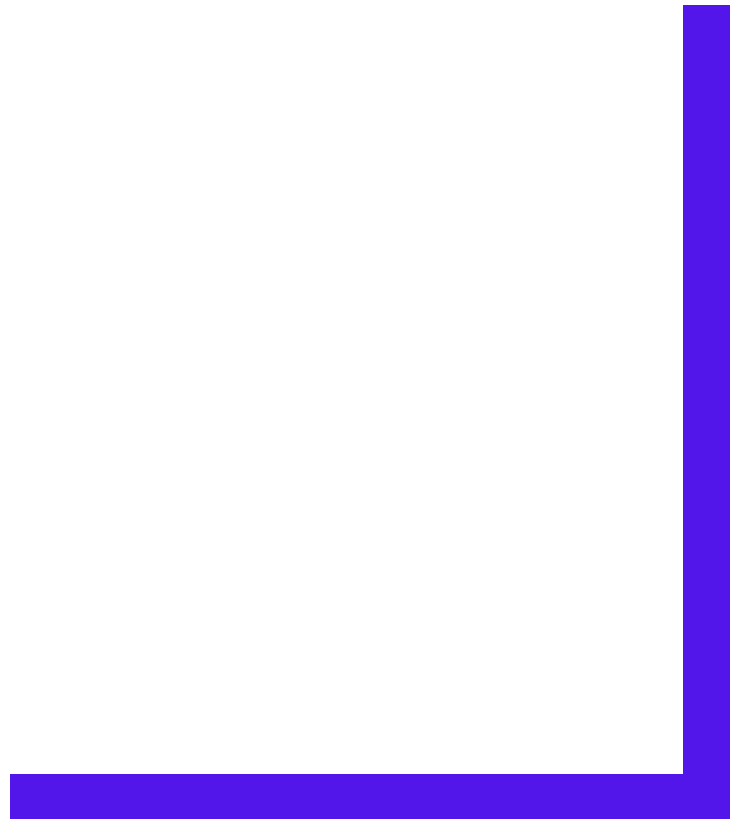
growth in the I-71 corridor or is the growth in the corridor creating fertile conditions for non-farm self employment. Of course, both are playing a role to some degree, but economists have a challenging time disentangling the two.⁷

Figure 2b shows that 2005 farm self-employment is more concentrated in northwest and southeast Ohio, and obviously, less concentrated in metropolitan counties. The intensity of farm employment seems to be unevenly distributed in Appalachian Ohio. Figure 2a shows that while Monroe, Morgan, and Noble Counties have between 9 and 12% of their total labor force working as self-employed farmers, this ratio is less than 2% in neighboring Athens County. Meigs and Vinton Counties in Southeast Ohio both experienced job losses between 1991 and 2005 (Partridge et al., 2007), but they also have some of the highest shares of farm self-employment. Neighboring Jackson County, with low shares of farm self-employment, fared much better in terms of total job growth in the same period. There are also cases such as Morrow county between Columbus and Cleveland that has high shares of both non-farm and farm self employment, in which Morrow County employment growth was about twice the state average between 1991 and 2005.

If researchers don’t fully understand the features of non-farm self employment and its linkages to broader economic conditions, they have even less understanding of farm self employment. Farmer operators were not always associated with being among the most entrepreneurial, especially in the era of rapid consolidation of farm operations when many farmers ceased operations. However, with farm populations more stabilized and farm sizes often quite large, operators are increasingly associated with significant business



savvy in managing large complex operations. This shift may have large impacts on many rural communities, but economists and policymakers still do not fully understand how to tap this entrepreneurial capacity for the broader rural economy. However, while economists are less clear about the broader community-wide benefits, they do increasingly understand how to maximize local agricultural entrepreneur capacity and the role of sustainable agriculture in promoting a healthy, attractive local environment (van der Ploeg, 2000; Marsden, 2004; Marsden and Smith, 2005).



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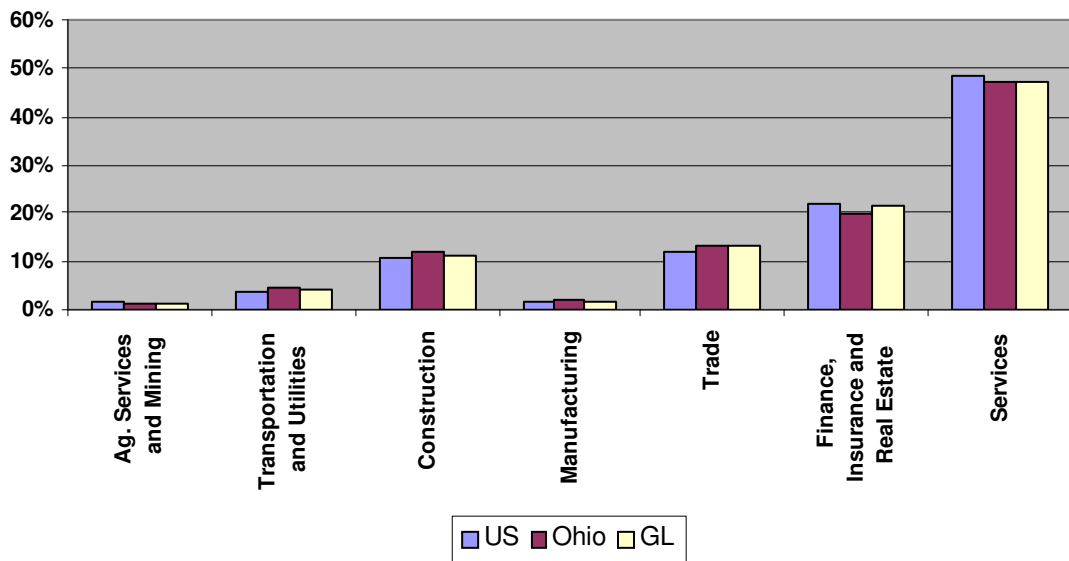
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Who are the Self Employed?

Figure 3a shows the distribution of nonfarm self-employed workers by sector in 2005. Most of the self-employed chose to work in Services, followed by Finance, Insurance and Real Estate. Few work in Agricultural Services & Mining, as well as in Manufacturing. Of course this partially reflects the fact that (broadly-defined) services are the largest sector in Ohio, while manufacturing and agricultural services employ a much smaller share.

Figure 3b accounts for the relative size of each sector by reporting the 2005 share of employment in each sector that is self-employed. In 2005, approximately 75% of U.S. farm employment was accounted for by the self-employed farm operators. The share of farmer operators is even higher in Ohio and the Great Lakes region (over 80%). Agricultural services and mining also had large shares of self-employed workers, followed by finance, insurance, and real estate. On the other hand, manufacturing had the lowest proportion of self-employment.

Panel A
Who are the Self-Employed?: The Distribution of Non-farm
Self-Employed Workers by Sector, 2005



Note: This graph shows the share of self-employed workers in each sector as a percentage of total self-employed workers in all sectors.

Figure 3a

Panel B
Who are the-Self Employed?: Non-farm and Farm
Self-Employment as a Share of the Sector Total Employment, 2005

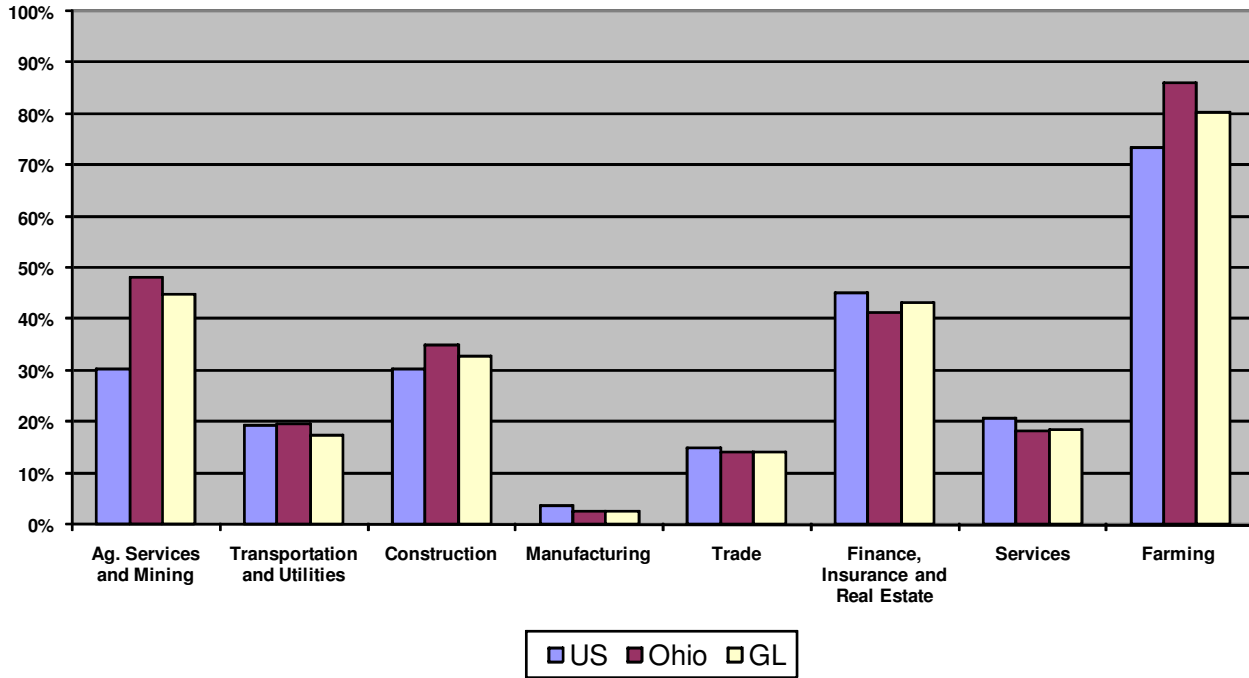


Figure 3b

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Growth in Self-Employment

Figure 4a shows that the number of non-farm self-employed workers in rural Ohio more than doubled between 1969 and 2005. However, unlike Pennsylvania and the Great Lakes region shown in Figure 4b, as of 2005, manufacturing jobs in rural Ohio still outnumber rural manufacturing sector remained steady at around 260,000, before experiencing a gradual and consistent decline in the past 5 years to around 220,000 in 2005. At this rate, the number of non-farm self-employed workers will be expected to soon exceed the number of rural-Ohio

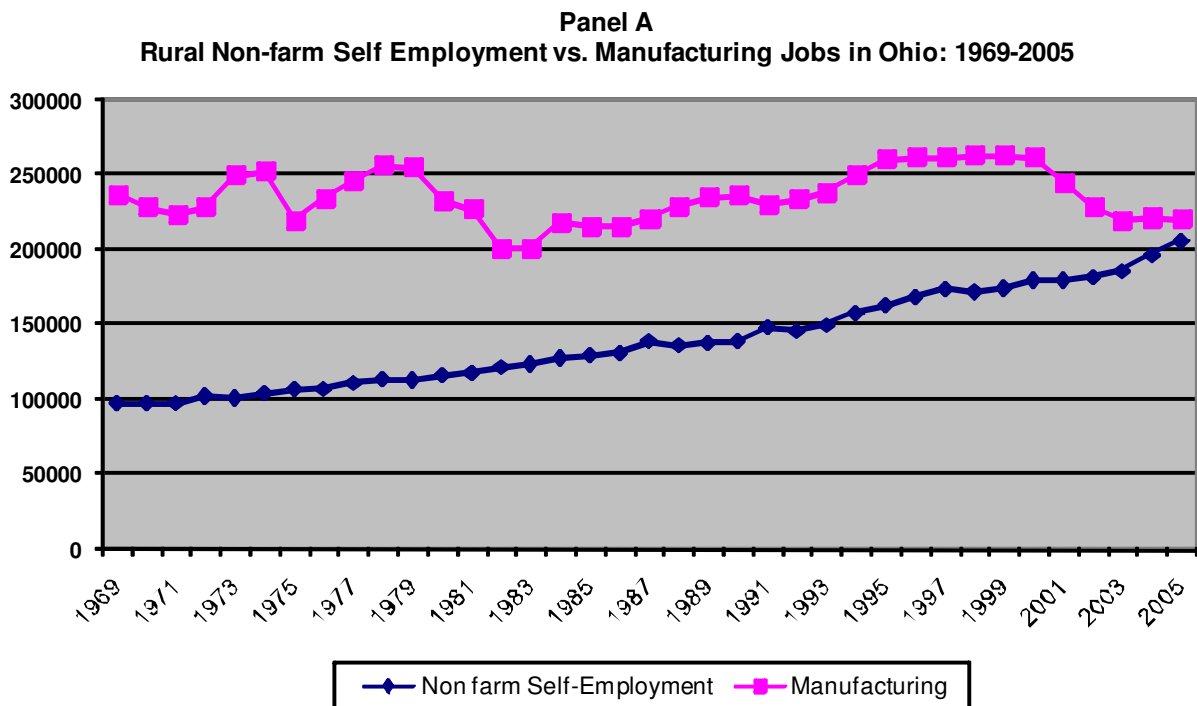


Figure 4a

non-farm self-employed workers. In 1969, the number of manufacturing jobs in rural Ohio was almost two-and-half times the number of self-employed workers, but by 2005, these figures were near par. During the mid 1990s, the number of jobs in the manufacturing workers. This illustrates why developing small businesses is one possible pillar in producing future economic growth in rural Ohio. To be sure, manufacturing will remain an important component of rural Ohio, especially with

**Rural Self Employment vs. Manufacturing Jobs in the Great Lakes (less OH):
1969-2005**

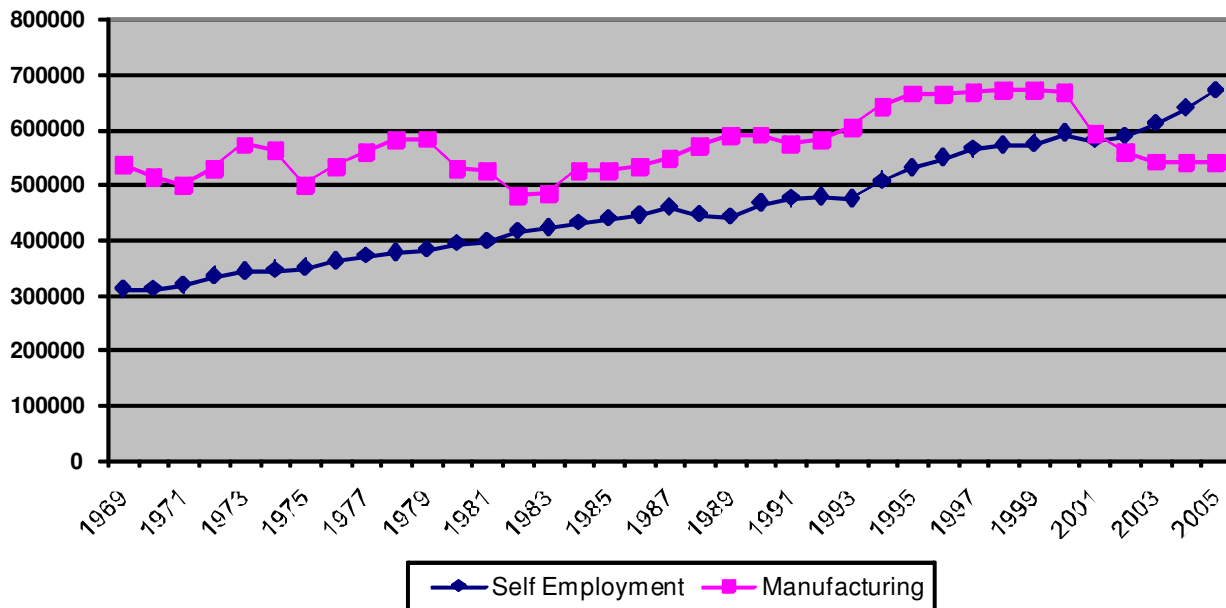


Figure 4b

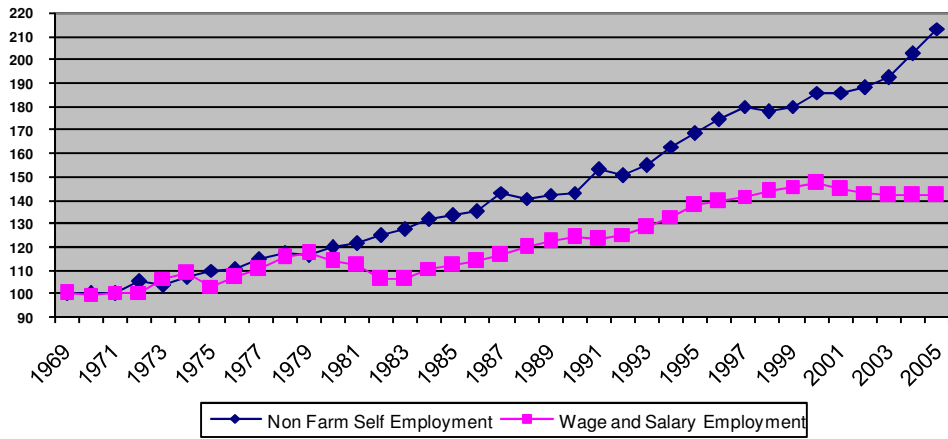
the weakening of the U.S. dollar, but Ohio's future growth prospects will likely have to rely on other sources.

The relative importance of self-employment jobs to rural Ohio and rural America extends well beyond its replacing manufacturing as the most important mainstay of the rural economy. More broadly, total wage-and-salary jobs have not increased as rapidly as the number of self-employed. Since 1969, Figure 5 shows that the number of wage-and-salary jobs rose by only 41 percent in rural Ohio and by only 54 percent in the rural parts of the neighboring Great Lake states. By comparison, self-employment rose by around 113 percent in both regions, which is well over double the pace of wage and salary employment. Especially, in rural Ohio, growth in self employment has been a key feature of long-term economic expansion.⁸ The share of non-farm self-employed in all jobs increased from 12.3 percent in 1969 to 18.1 percent in 2005 in rural Ohio.⁹ Reflect-

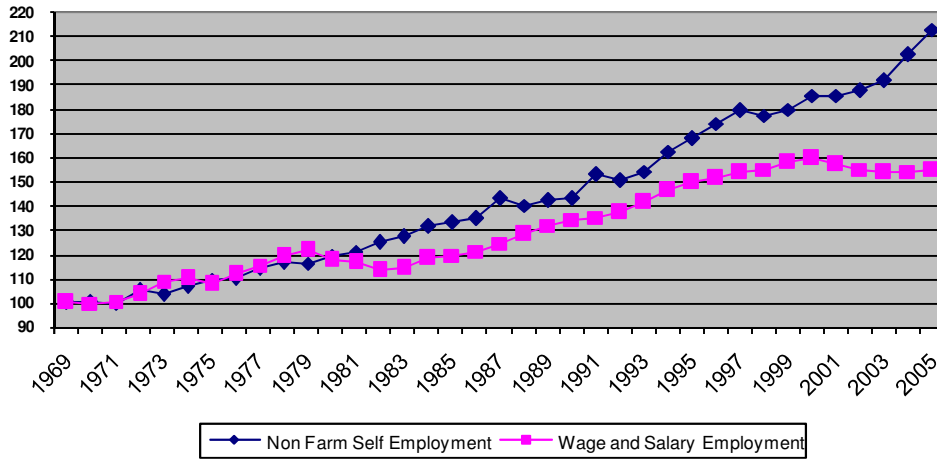
ing farm consolidation, over this span, farm self employment fell by 27 percent in rural Ohio, 34 percent in the rural Great Lakes region (without Ohio), and 26 percent in the rural U.S. as a whole. Though farm self-employment declined over this period, this shows how rural areas are diversifying in terms of self employment, which should make them less vulnerable to economic declines.

The trend towards self-employment representing an ever important role in rural Ohio appears to be accelerating. Figure 6a shows that the total number of wage and salary jobs fell in Ohio and the Great Lakes between 2001 and 2005, while self employment increased over 15 percent during the period. Figure 6b shows a similar pattern for rural regions. The clear point is that without rapid growth in self employment since 2000, overall job growth would have been near zero.

Panel A
Rural OH non farm self employment vs. rural OH wage and salary employment
 [1969 = 100]



Panel B
Rural Great Lakes (less OH) non farm self employment vs. rural Great Lakes (less OH) wage and salary employment
 [1969 = 100]



Panel C
Rural US non farm self employment vs. rural US wage and salary employment
 [1969 = 100]



***Notes:** The base year is 1969, i.e. the employment indices are normalized to 100 in 1969. In all subsequent years the index is calculated as (Employment in year xxxx)/(Employment in 1969)×100

Figure 5

Panel A
Growth in Total Wage and Salary Employment and
Total Ohio Self Employment: 2001-2005



Panel B
Growth in Rural Wage and Salary Employment and
Rural Self Employment: 2001-2005



Figure 6

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Does Self Employment Create High Paying Jobs?

Even though the number of self-employed workers has risen faster than wage-and-salary jobs in rural Ohio, the relative returns for self-employment have declined over time. Figure 7 shows that in 1969, average returns to self-employment were modestly higher relative to wage-and-salary work in rural Ohio, but by 2005, this return fell to 49 percent of average wage-and-salary earnings. In other words, the typical self-employed rural worker today earns about one-half as much as the typical wage-and-salary worker (compared to 4 percent more 35 years ago).

In the Great Lakes region, returns to rural self-employment took an even greater dive. In 1969, (nonfarm) self-employment in the rural regions of the Great Lakes was 17 percent more profitable than wage-and-salary jobs. Between 1969 and 2005, however, the relative return fell to about 52 percent of a typical wage and salary job. Panel C shows a similar pattern for returns to rural U.S. self employment over the time period.¹⁰

Figure 7 illustrates that another pattern is the reversal between metropolitan and non-metropolitan areas. In 1969, relative returns

Panel A
Returns to Non Farm Self Employment Relative to Wage and Salary Employment, OH 1969 and 2005 [Wage and Salary = 1]

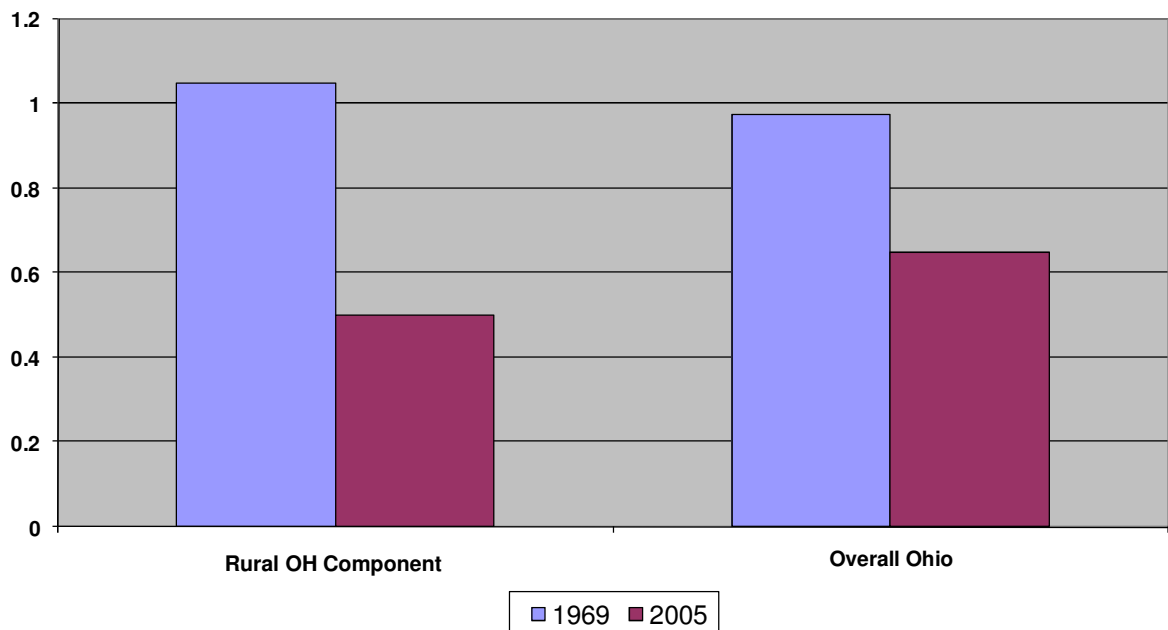
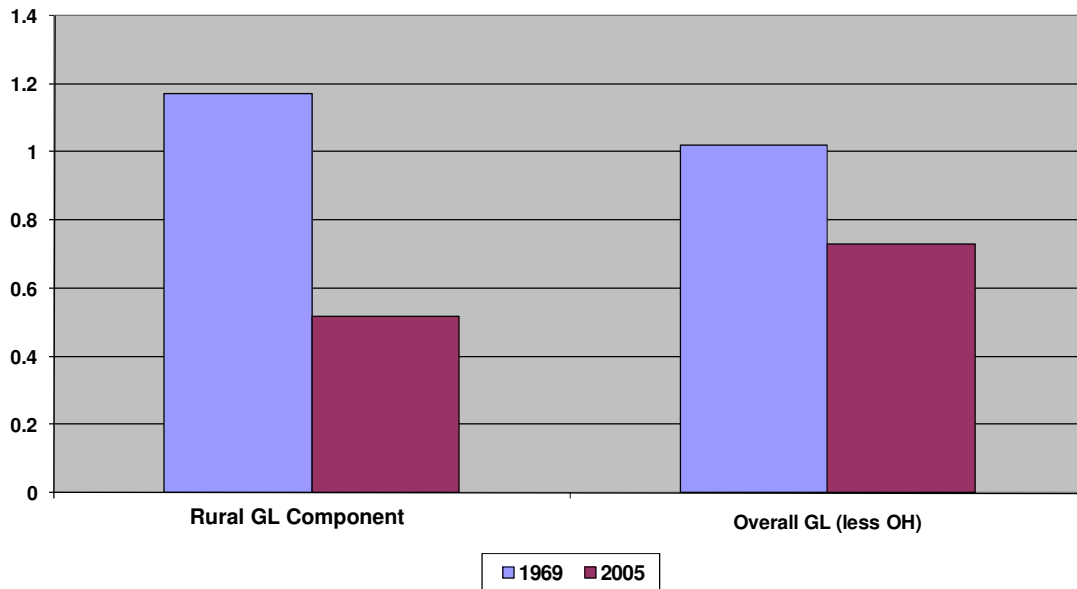
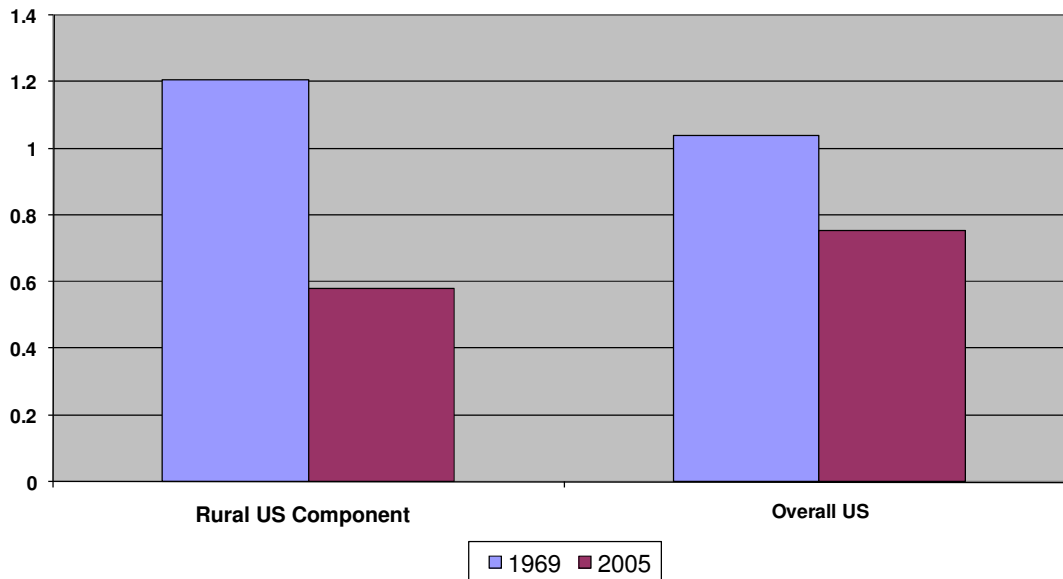


Figure 7a

Panel B
Returns to Non Farm Self Employment Relative to Wage and Salary
Employment, Great Lakes (less OH) 1969 and 2005 [Wage and Salary = 1]



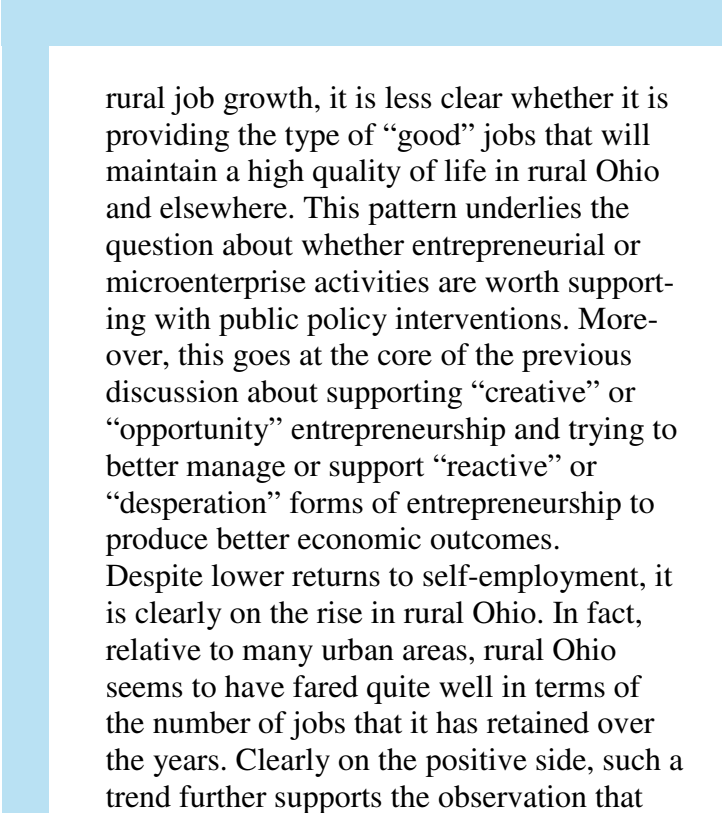
Panel C
Returns to Non Farm Self Employment Relative to Wage and Salary
Employment, United States 1969 and 2005 [Wage and Salary = 1]



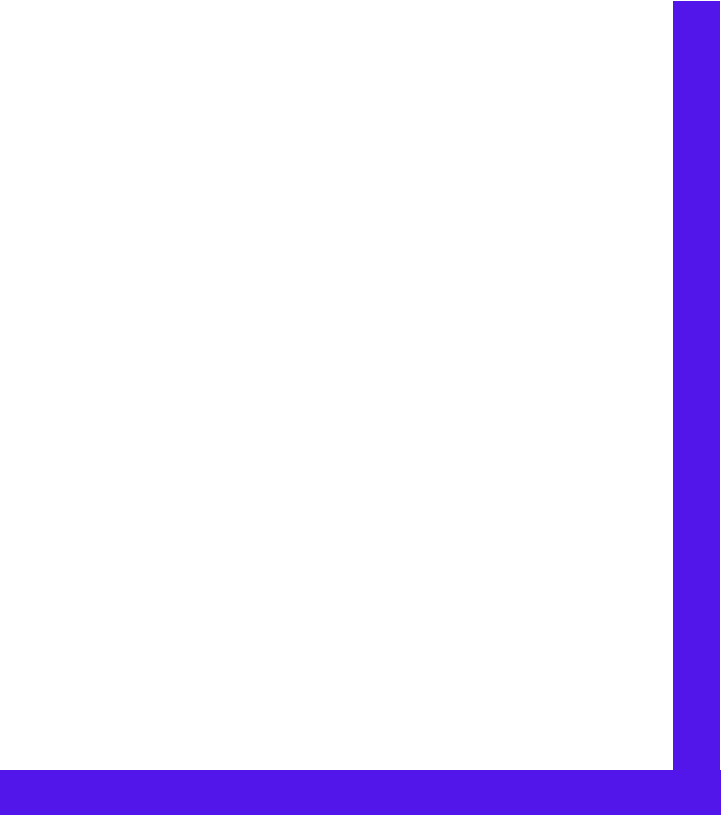


Figures 7b and 7c

to nonfarm self employment were higher in rural areas compared to metropolitan areas. However, this had greatly changed by 2005. In Ohio, metropolitan self-employment returns were about 68 percent of the typical

metropolitan wage and salary job in 2005, while this ratio was in the 70 to 80 percent range in the Great Lakes region and the U.S. An implication is that while self employment appears to be a key factor in supporting



rural job growth, it is less clear whether it is providing the type of “good” jobs that will maintain a high quality of life in rural Ohio and elsewhere. This pattern underlies the question about whether entrepreneurial or microenterprise activities are worth supporting with public policy interventions. Moreover, this goes at the core of the previous discussion about supporting “creative” or “opportunity” entrepreneurship and trying to better manage or support “reactive” or “desperation” forms of entrepreneurship to produce better economic outcomes. Despite lower returns to self-employment, it is clearly on the rise in rural Ohio. In fact, relative to many urban areas, rural Ohio seems to have fared quite well in terms of the number of jobs that it has retained over the years. Clearly on the positive side, such a trend further supports the observation that residents are attached to their communities and are willing to trade off a little income for a higher quality of life (Partridge et al., 2007). However, unless measures are taken to improve the productivity of the self employed and other rural workers, more rural Ohioans may eventually leave the state, or their children may find less reason to remain in rural Ohio. Thus, Ohio would be well versed to find ways to improve the performance of its microenterprises and self-employed to produce higher returns.



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January 2008

Supporting Entrepreneurship Through Innovation

A clear way for Ohio to increase its productivity is to have high levels of creativity and innovation. One avenue for this to occur is when new innovations are taken from the “laboratory” to the market through self employment or microenterprise (or supporting the expansion or retention of existing businesses). Of course, a necessary step for this to occur is for Ohio to produce new innovations and provide support to get these innovations to the market *via local* businesses that retain more jobs and profits.

In assessing how well Ohio is doing in fostering an environment of creativity and innovation, Figure 8 shows that the state is lagging its neighbors. In terms of total patents, Ohio 29th ranking trails Pennsylvania and especially Michigan. Indeed, because innovative activities are associated with cities (Carlino, 2001), Ohio's performance greatly trails what would be expected in one of the most urbanized and populous states (i.e., Ohio is the 7th most populous state). Likewise, in terms of efforts to fund new and/or innovative enterprises, Ohio also lags the national average and its neighbors in terms of initial public offerings and venture capital funding. Finally, in terms of key inputs, Ohio trails in terms of the number of scientists and engineers and R&D investment—where again, the pattern underperforms what would be expected for a very populous state.

The clear pattern is that if Ohio wants to

support high-paying and profitable new enterprises, it currently lacks the underlying foundation that would sustain such efforts. Indeed, with Ohio's long-term struggles, these figures support the observation we made in our last policy brief that the underlying business climate is critical (Partridge et al., 2007). Foremost, one of the problems that Ohio faces is changing long-term expectations. Entre-

Ohio Innovation and Creativity: Ranking Among States [1 = highest state]

	OH	PA	MI
Population*	7	6	8
Patents	29	22	15
IPOs	32	18	30
Venture Capital	35	14	34
Scientists and Engineers	24	14	25
Industry Investment in R&D	19	13	4

Figure 8

Source: Kauffman Foundation, 2007 available at http://www.kauffman.org/pdf/2007_State_Index.pdf

* Source: US Census Bureau at <http://www.census.gov/>

Notes: Indicators are measured by number of patents issued; the value of initial public stock offerings (IPOs) by companies; venture capital activity; the number of scientists and engineers in the workforce; and industry investment in research and development.

preneurs, talented young professionals, and investors are reluctant to locate in places that are expected to underperform the nation. Ohio needs to change that dynamic if it wants to score higher in innovation indicators and then subsequently in job and wealth creation.



Growth and Change:

Does Enhancing Ohio's Small Businesses and Entrepreneurs
Provide the Key to Growth?

The Ohio State University

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Policy Implications and Suggestions

Self employment is often claimed to be one of the best development tools for rural and urban America. Especially in rural areas, it captures the notion that less-densely settled areas should “grow from within” by encouraging local entrepreneurship and retaining and expanding existing businesses. This reflects the view that “smokestack chasing” and tax abatements are less likely to be successful because by definition, they are often a zero-sum game where each winning jurisdiction is offset by a losing jurisdiction (Peters and Fisher, 2002, 2004).

Though encouraging entrepreneurship seems sensible, there are some caveats that apply before a full-court expansion of government policies to promote microenterprises and self employment. Probably the biggest drawback to such an effort is that many of the self employed earn a relatively low salary, though there may be an income tradeoff for being their own “boss” (Partridge, 2002). Moreover, communities are more likely to benefit from self employment and new business start-ups if they are not of the reactive or desperation form. Yet, because “creative destruction” is an important force, how can government help ensure that these reactive forms of entrepreneurship produce better community outcomes?

With these principles in mind, we make the following policy suggestions.

State and Local Government Efforts

- The best way to provide a good climate for small business start ups is to have a strong Ohio economy. Past policy briefs outline some possible ways for the state government and local governments to enhance the economic climate including efforts to reduce the tax burden by providing efficient services that are not duplicated by other jurisdictions. Regionalism is one possible way to reduce the costs of government and provide coherent economic development.
- The state needs to better understand the evolving forms of business start-ups. *For example, what are the most effective ways to encourage start-ups and how should these strategies vary from rural to urban Ohio?* Successful business start-ups in rural areas will likely differ from urban areas. Should Ohio encourage incubators in smaller urban areas and rural communities to provide support to local entrepreneurs? Alternatively, should Ohio provide additional support and training of new businesses? Because there is much that is still unknown about entrepreneurship, the point is more cost-effective services can be provided if more research and assessment is done.
- The state through the Department of Development and related agencies such as Ohio Environmental Protection Agency should continuously strive to streamline regulatory processes and reporting burdens of small businesses. This also follows for local governments. The aim should not be to cut corners for regulations, but to recognize that small businesses have less capacity for reporting. In this global economy, small changes in costs can make Ohio's small and large businesses more competitive.
- State and local governments should be very cautious in providing tax incentives and grants (Peters and Fisher, 2002, 2004; Partridge and Rickman, 2006). Specifically, a tax incentive or a grant generally implies that the remaining businesses and residents have to pick up the tax burden. Of course, small businesses are often less likely to benefit from these type of incentives, meaning they would disproportionately pay for them through higher taxes or reduced services. Given the tenacity of market competition, small businesses would generally be the most sensitive to such changes in cost structure. Thus, unless the tax incentive has broad-based community impacts such as cleaning up brown fields to put them back on tax roles, such policies should be very cautiously applied.
- State and local governments should try to reduce some of the barriers to entrepreneurship. For example, one potential barrier to being self employed or being a small business owner is the affordability of health insurance. Steps to reduce the costs of health insurance would mitigate this effect.
- Ohio's state and local governments should work to build the necessary infrastructure for the state's emerging entrepreneurs. In rural Ohio, that often relates to facilitating the development of broadband service and enhancing efforts to provide better access to venture and bridge capital.

Workforce Training and Ohio's Educational Institutions

- Small businesses need access to good workers, implying a need for the state and local governments to provide better workforce training and education. Ohio should facilitate innovative activities by supporting strong educational establishments and non profit research institutions (e.g., Battelle and the Cleveland Clinic) by provide adequate research support. Recent state efforts to support research including the Third Frontier are good starts. Yet, more effort is needed to ensure that these lead to successful *new* business endeavors. Likewise, the state needs to allow researchers enough freedom to innovate across a wide range of topics. Though governments and bureaucracies can provide fertile conditions for productive research by providing adequate funding, they are much less likely to be good scientific committees that direct researchers towards the emerging 21st Century technologies.
- Ohio's community colleges and universities should consider devising an integrated series of course work to show individuals how to start a business and identify market opportunities.¹¹ Assuming funding is adequate, the coursework would be uniform and describe marketing, accounting, legal issues for new and existing business owners. Individuals who successfully complete this coursework and training would be certified as (say) a *Buckeye Entrepreneur*. Of course, such a process can be found in a variety of settings, but they tend to be more *ad hoc*. What is more unique is the suggestion to formally provide a statewide certification process. Such a training process would then be more recognized in the region. Moreover, once the microenterprise training process becomes more formalized in educational settings, then the training will be more standardized and subject to continuous revision to better reflect changing best practices.
- Ohio's universities should continue to find ways to take new innovations to market. Efforts have been made in this direction, but further focus on how to streamline and facilitate this process would be helpful in producing more entrepreneurial opportunities.
- Knowledge and creative workers are not just attracted by strong economic conditions, but also a strong quality of life (Florida, 2002; Adamson, et al., 2004). Ohio's state and local governments should incorporate quality-of-life initiatives as part of any knowledge and creative worker endeavor or innovation strategy. These initiatives should tap the state's abundant natural and man-made assets.



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Summary

Ohio's economy has lagged the national average as well as its neighboring Great Lake States for the last few decades. Simple solutions are unlikely to break this pattern. Yet, one possibility is to encourage more entrepreneurship and innovation, while trying to grow Ohio's communities "from within." Focusing on locally grown talent seems most sensible for Ohio's rural communities and smaller cities. Indeed, we find that a significant component of new job formation in Ohio since the 1960s is self employment—with self employment being the main reason for positive net job creation since 2000.

Unlike other indicators, Ohio's growth in self employment is not significantly behind other Great Lake states, but it does lag the national average. However, one caveat is that the average earnings among the self employed greatly lag the average wage and salary earner, especially in Ohio. One likely contributing factor is that many of those who start businesses do so out of desperation rather than as result of a compelling business plan or a novel idea. Though there are many benefits of a dynamic entrepreneurial climate, the relative low wages among the self employed is one reason why we don't view enhanced self employment or greater reliance on micro enterprises as a panacea.

All forms of Ohio business would likely benefit if the state could improve its woeful performance in terms of innovation. Fortunately, in this regard, across the state, there are key assets to build on, including excellent research universities, research institutions and health-care facilities. Yet this will require leadership in the business, government, nonprofit, and academic communities. One key factor will be to change the expectations about Ohio's economic future to attract financial investment and new creative and knowledge workers.

End Notes

1. Carton, et al. (1998) provide a working definition of entrepreneurship as "...the pursuit of a discontinuous opportunity involving the creation of an organization (or sub-organization) with the expectation of value creation to the participants. The entrepreneur is the individual (or team) that identifies the opportunity, gathers the necessary resources, creates and is ultimately responsible for the performance of the organization. Therefore, entrepreneurship is the means by which new organizations are formed with their resultant job and wealth creation." (see Anderson, 2002 for the exact quote).
2. This policy brief has greatly benefited from discussions with Stephan Goetz of Pennsylvania State University. Much of this brief follows similar work Goetz has done for Pennsylvania.
3. The Small Business Administration defines a small business as having fewer than 500 employees.
4. See Georgellis and Wall (2000, 2006) for more discussion of the determinants or causes of self employment.
5. In this policy brief, we will follow convention and interchange the terms "rural" and "nonmetropolitan" throughout the analysis.
6. In 1969, self employed workers accounted for 12.4% of Delaware County's total employment, which was above the corresponding 9.0%, the 1969 state average in metropolitan areas. Thus, higher intensities of self employment *may* be one reason for Delaware county's subsequent success.
7. For Ohio's 88 counties, the correlation between the 1990 share of nonfarm employment that was self employed and subsequent 1990-2005 *nonfarm* wage-and-salary employment growth was 0.33. This association is consistent with greater self employment intensities supporting future job growth, but correlation is not causation.
8. Between 1969 and 2005, U.S. rural wage and salary employment grew by 62%, while U.S. rural self employment grew by 143%.
9. The corresponding self-employment shares for the Great Lakes (without Ohio) and the U.S. are 13.9% and 13.5% in 1969 and 19.5 % and 20.1% in 2005.
10. Of course, bear in mind that this average includes part-time self employment, which is also the case for wage and salary employment.
11. Two examples of Ohio's universities trying to foster more successful small businesses are the incubators at the OSU South Centers Endeavor Center in Piketon <www.endeavor.osu.edu/> and OSU's incubator kitchen at the John E. Hirzel Sustainable Agriculture Research and Education Site <www.agincubator.org/AIF/projects2.html>.

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Ohio Reference Map

