

A Quick Read on the State of Small Business and the Small Business Success Index

June 2009 Survey of Small Business Success

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Sponsored by: **Network Solutions, LLC and the Center for Excellence in Service at the University of Maryland's Robert H. Smith School of Business**

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Introduction

The current global economic downturn, the worst since the Great Depression, is transforming the way businesses in the United States operate. For America's 6 million small businesses that maintain payrolls, this economic environment is creating challenges to their basic well-being and survival never before seen by today's owners. Yet, as workers in the general economy watch unemployment soar and worry about their jobs, the owners of small businesses are basically satisfied with their vocation. Even while they make tough choices and struggle to compete, owners of small business are making their operations more efficient and finding innovative ways to meet customer needs. Small business optimism is rising, and if owners are correct, this sector can look forward to a bright future.

Because of the importance of the small business sector, which accounts for over one out of every three jobs in the U.S., Network Solutions, LLC and the Center for Excellence in Service at the University of Maryland's Robert H. Smith School of Business have partnered to track the competitive health of small businesses over time. The survey is conducted by telephone and the first survey wave (Wave 1) was fielded in December and January among 1000 small businesses. The second survey wave (Wave 2), reported here, was conducted in June with 500 small business owners, providing a six month trend line. (The methodology is discussed in greater detail in the last section of this report, *About the Small Business Success Survey*.)

Competitiveness in this study is defined as the level of success a small business achieves in conducting the organizational activities critical to its short and long term viability. The more competitive a small business is, the more likely it is to meet the personal and business goals of its owners and show positive financial results. The Small Business Success Index (SBSI) is composed of 6 distinct dimensions, as shown in the competitiveness report card in Figure 1.

Figure 1

Small Business Success Report Card				
	Importance Score**	Index Score*	Grade	✓
OVERALL INDEX SCORE*		75	C	➡
Sub-Indices				
Capital Access	33	69	D+	⬇️
Marketing & Innovation	23	70	C-	⬇️
Workforce	14	78	C+	⬆️
Customer Service	11	91	A-	⬆️
Computer Technology	11	75	C	➡
Compliance	8	89	B+	⬆️
*Index Score is calculated on a 0-100 scale				
**Importance Score is calculated proportionally, meaning that the total of the numbers across all the sub-indices is 100%.				

The SBSI ranges from 0 to 100, and is currently 75, which can be viewed as a "solid C". This level is unchanged from 6 months ago, and other data reported here suggest that a deepening recession has restrained the ability of small businesses to improve their situation. Out of 28 competitive dimensions that make up the index, the only one that has changed significantly is the ability to provide attractive benefits to employees, and this has declined. This wave of the SBSI provides considerable detail on how the economy is affecting small businesses and how they are responding.

A major obstacle small businesses face today is in the highly important area of capital access, which consists of a small business' ability to meet short and long range financial needs. The report for this wave sheds light on this problem, with details on how small businesses finance their needs and how the capital crunch affects owners personally.

This wave of the SBSI also provides depth on other issues that are prominent in the national debate on America’s future, including employee benefits, healthcare and regulation. The report for this wave details what kinds of benefits small businesses are able to offer, how this has changed in the recession, and what problems they face in providing affordable healthcare. This study also provides more detail on regulation and where it has the greatest impact on small business (included in full report).

Capital Access for Small Businesses

Capital Access is small businesses’ weakest area, with success equating to a “D+,” even though it is the most important one to succeed in to be competitive. In this recent survey wave, small business owners were asked about the issue of capital access directly:

- The majority, 70 percent, believe their access to working capital is sufficient to meet their needs today, but 30 percent believe the capital is not sufficient¹
- Almost a third – 34 percent – believe their lack of access is impeding their growth.²

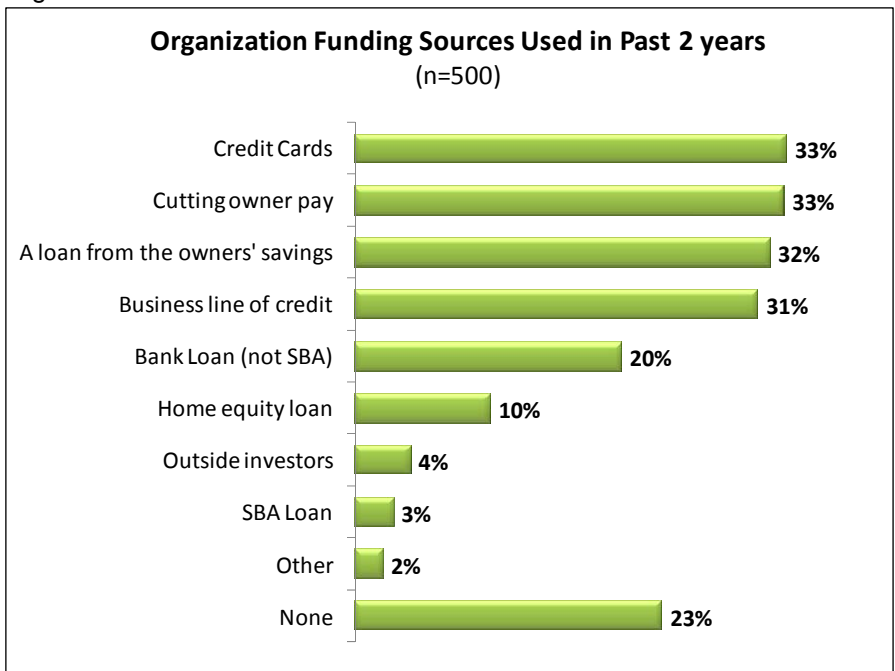
While a majority considers their capital needs sufficient, there is an endemic problem when a third is not able to meet their needs on a fundamental criterion for business success.

How do small businesses meet their financing needs? Aside from cash on hand, the two most common sources over the past two years have been credit cards (33 percent), cutting the owners’ pay (33 percent), and a loan from the owners’ savings (32 percent) (see Figure 2). Small business owners often serve as their own “banks” to meet their financial needs, cutting their pay or dipping into savings. The effect of the economy on this behavior is reinforced by the fact that business owners that did not show a profit last year are far more likely to rely on credit cards, their own pay or personal savings for capital.

Another third rely on traditional bank lines of credit and a fifth get loans from a bank (not SBA). The image of the small business as an entrepreneurial firm relying on investors and SBA loans is far from reality, as these sources are rarely used.

Over half of small business owners have noted that at least one of these sources has been disappearing in the past year, and the share of small business owners citing various sources as going away is typically almost as high as the share who used the source. The most commonly cited sources to have “become scarcer or vanished” in the past year are

Figure 2



¹ Is your working capital sufficient to your business today? Yes, No.

² Is access to capital impeding your growth objectives? Yes, No.

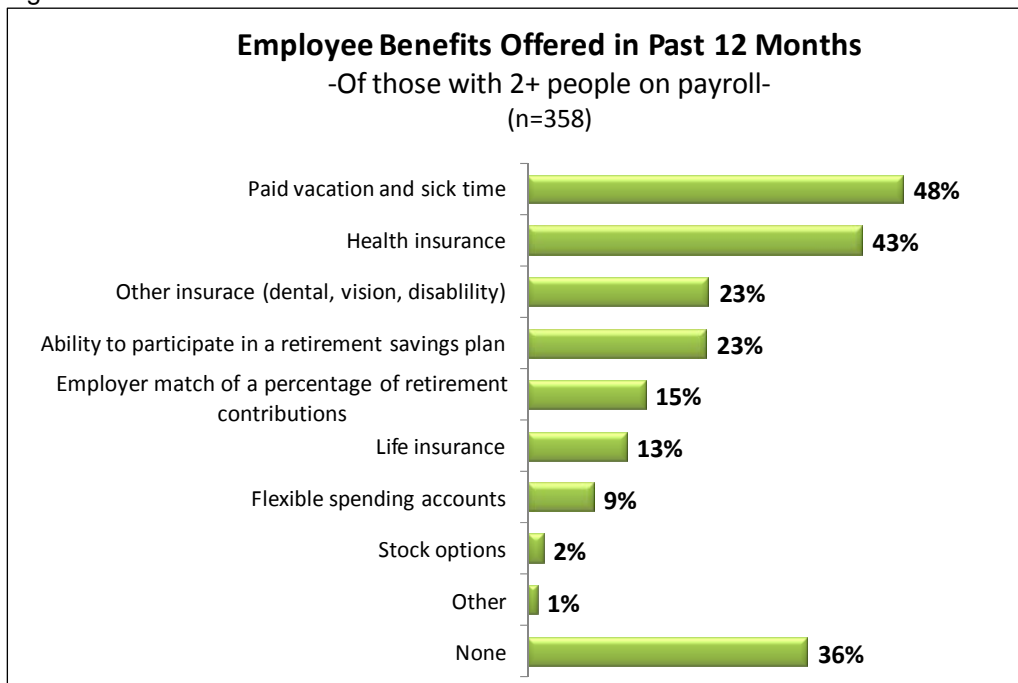
also the most common sources used in general, and include: a loan from the owners' savings (21 percent), credit cards (20 percent), cutting owner pay (16 percent) and a business line of credit (15 percent). It seems that as the recession deepens, owners are starting to deplete their own reserves, running out of savings and unable to cut pay further.

Workforce and Benefits Issues

Compared to Capital Access and Marketing and Innovation, small businesses perform somewhat better in the Workforce area, with a 'C+' score. Problems in this area, which includes morale and benefits, have a broad social significance because 70 percent of small businesses have two or more persons on their payroll, and the small business sector accounts for 36 percent of jobs in the U.S.³

Before discussing the challenges of providing benefits, it is worth noting which benefits small businesses offer now or have offered within the past two years (see Figure 3). Although there has been no benchmarking with large companies, it seems that small businesses do not offer a plethora of benefits, with 36 percent of companies with two or more people on payroll reporting they have offered no significant benefits in the past 12 months. Among those with two or more people, about half (48 percent) have offered paid vacation and sick time within the past 12 months. Only 43 percent offer or have offered health insurance, and barely a quarter (23 percent) offer enhanced insurance such as dental or disability. Just under a quarter (23 percent) of small businesses have offered the ability to participate in any kind of retirement or savings plan such as a SEP-IRA or 401K, but fewer (15 percent) offer retirement plan matching.

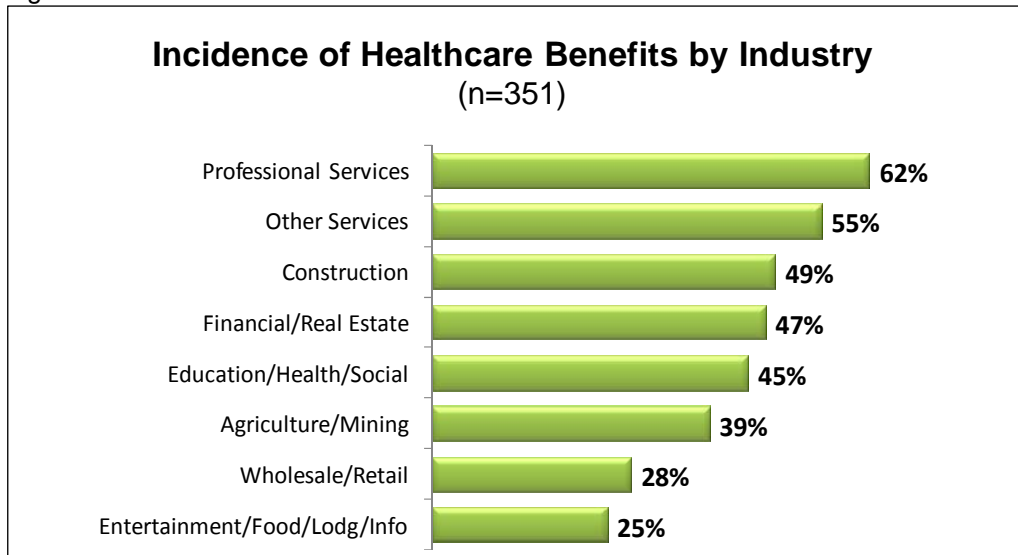
Figure 3



³ Source is the U.S. Census Bureau, 2006 Statistics of U.S. businesses (SUBB).

The level and nature of benefits varies by industry and reflects the industries and workforces of the businesses. For instance, health insurance is offered by 62 percent of professional services firms, but only 25 percent of those in entertainment/food/lodging industries (see Figure 4). To illustrate, a small law practice may need to offer benefits to attract employees, while a restaurant may not have to because it has a more transient workforce.

Figure 4



There are a number of possible explanations for why small businesses do not offer a great deal of benefits. First, the size of the employee base may hinder the ability to shop for affordable benefits plans. Only 13 percent of these businesses have 20 to 99 employees⁴, and another 20 percent have 10 to 19 employees. Half (50 percent) of the businesses with just 2 to 4 employees do not offer any of the benefits covered in this study; only 31 percent of these small companies offer health insurance, compared to 75 percent of those with 20 to 99 employees.

Another factor may be that employees in many small businesses can receive benefits elsewhere, such as coverage through a family member, and would therefore prefer higher cash compensation. However, the most important reason may be the escalating costs of providing certain benefits which is affecting the owners as well as their employees (discussed in more detail below).

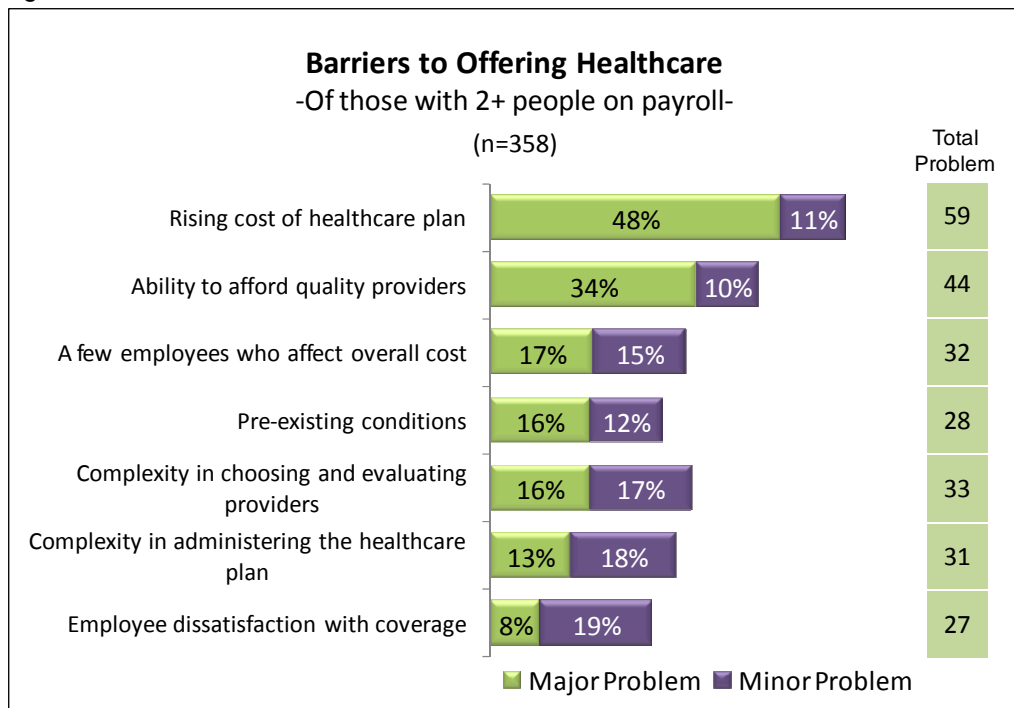
The level of benefits has changed in the past 12 months, with some being decreased or cut completely. The biggest benefit cut has been in retirement and savings plans. Among those who offered such plans, 15 percent have reduced their benefits and 3 percent have cut them completely, compared to 8 percent who expanded this benefit. Among those with employer matching, 14 percent have cut this benefit, while only 1 percent increased it.

Health insurance is a benefit that has seen a lot of change in the past 12 months, with two out of five small businesses either increasing (19 percent) or decreasing the benefit (22 percent) level. This study did not specifically ask what the changes in health coverage were, but it is likely that most of the “increases” consisted of absorbing price rises in coverage.

⁴ Businesses with 100 or more employees were not included in the study.

The most widespread problem small businesses face with providing healthcare coverage is the rising cost of plans (see Figure 5). Half (48 percent) of those with two or more people on payroll cite rising costs as a “major problem” and only 27 percent do not consider this a problem. The next major issue is the ability to afford quality providers, a major problem to 34 percent. A range of other issues exist, although none stand out as more important than others. These include the impact of a few employees on plan costs, the complexity of choosing and evaluating providers, and pre-existing conditions. The least problematic issue is employee dissatisfaction, so perhaps employees are just happy to have this benefit.

Figure 5



Computer Technology

Small businesses perform at a ‘C’ level on Computer Technology, but this area is of average importance to overall competitiveness. Small businesses could do better in taking advantage of technology in their businesses to run more efficiently, but have less trouble making it work effectively for them.

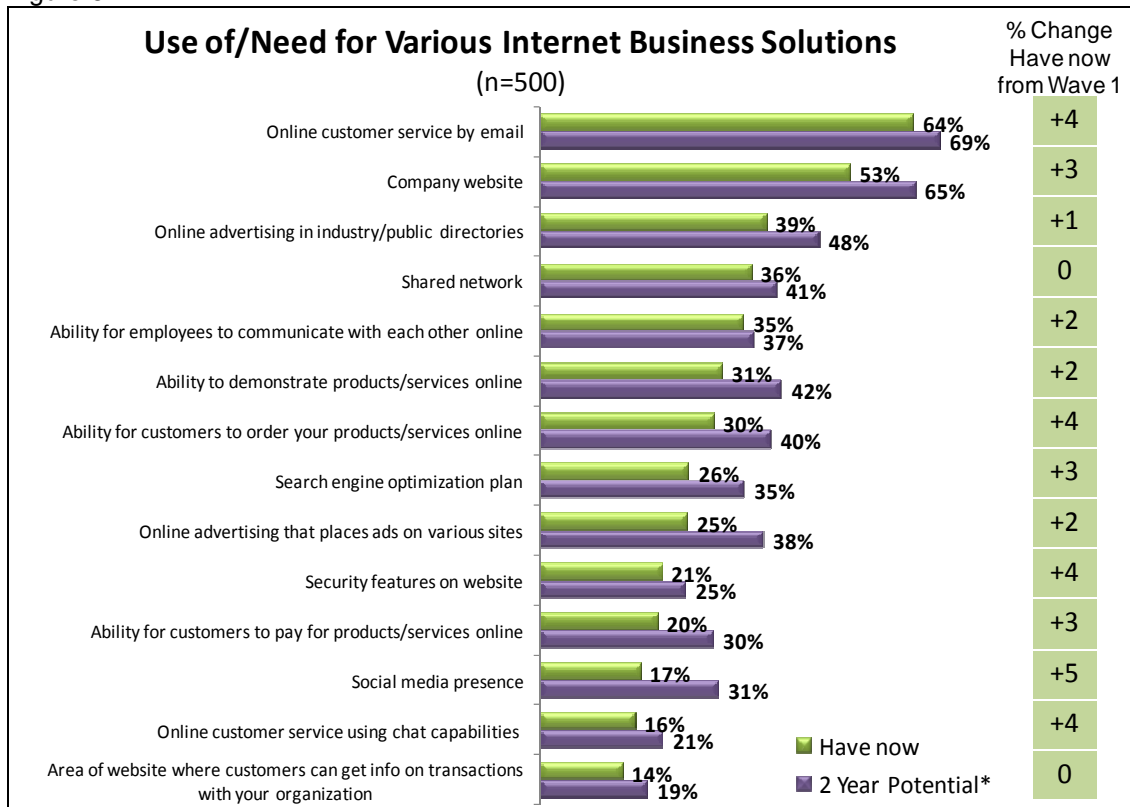
Which Internet technologies are small businesses making use of today? The most widely-used Internet technology and the one with the highest potential usage is online customer service via email (see Figure 6). Two out of three (64 percent) small businesses employ this, and another 5 percent want to have this capability within two years, for a potential total of 69 percent⁵. The next most prevalent technology is a company website, which is deployed by half (53 percent) of small businesses, but has a longer term potential of 65 percent (11 percent plan to get one in the next two years). The number using email is higher than the number with websites, indicating

⁵ Long-term potential is estimated by adding the percentage of those using the technology now to the percentage not using but planning to obtain in the next two years. In some cases, the potential estimate is 1 point different from the sum due to rounding error.

that many small business owners may use email providers like AOL, yahoo or gmail as their business email account.

In the past six months, the use of internet business solutions has spread, with the incidence of use of 12 out of 14 technologies increasing. The six month increases have been modest, ranging from 1 to 5 percent. The technology with the greatest increase, and the only one that is statistically significant, is the use of social media. The incidence of social media grew by 5 percentage points to 17 percent. As discussed in the full report, there is no evidence that social media is related to competitive success.

Figure 6



*Includes those who have now plus those planning to within 2 years.

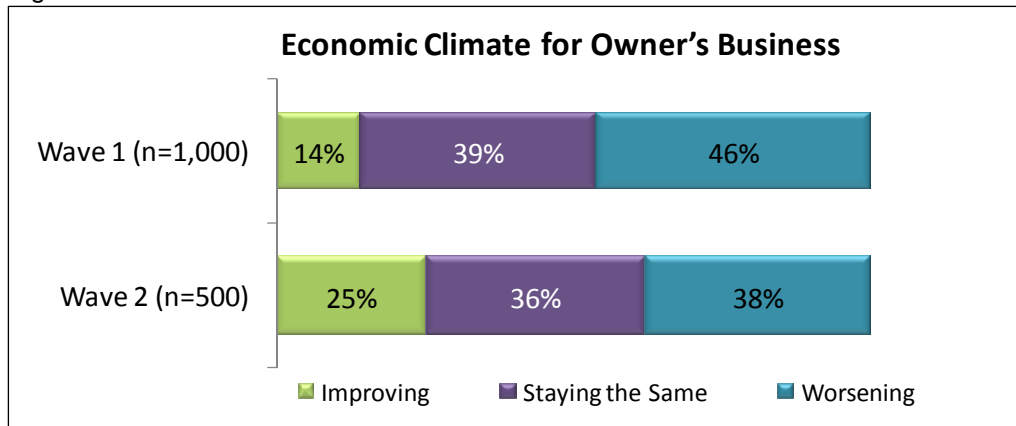
Owner Satisfaction

The ultimate measure of success for a small business is the degree of satisfaction with being a business owner. Almost two out of three (63 percent) small business owners are highly satisfied, rating their satisfaction 8, 9 or 10 on a 0 to 10 point scale (where 10 is completely satisfied). A third (32 percent) is moderately satisfied and only 5 percent are dissatisfied. Satisfaction is 86 percent among businesses considered highly competitive on the SBSI and only 40 percent among those who are failing on the index. Interestingly, even among the failing enterprises, only 11 percent are dissatisfied with being an owner. This high level of satisfaction, despite failing to meet so many personal goals (see full report) and economic problems (discussed later), is telling about the commitment of America's small business owners. They by and large enjoy what they are doing.

The Small Business Economic Climate

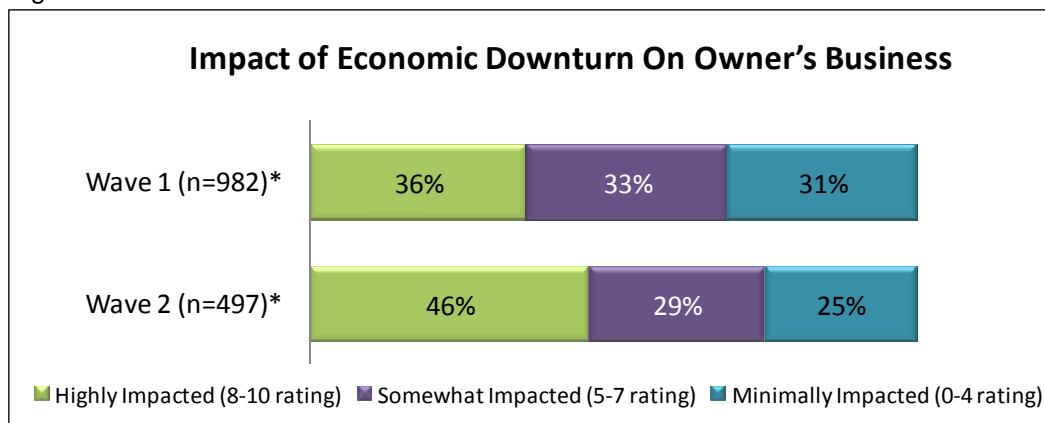
The SBSI was started six months ago when small businesses were in the midst of the current recession. Back in December/January, close to half (46 percent) of small-business owners felt the economic climate for their business was getting worse, while only 14 percent believed it was improving (see Figure 7). The outlook in June has improved with fewer believing the climate is worsening (38 percent) and a quarter (25 percent) now believing it will improve. Despite this brighter outlook, more small-business owners still believe the climate is worsening than improving.

Figure 7



The negative outlook six months ago has translated into reality today. Six months ago, a third (36 percent) of small businesses believed their business had been highly impacted by the economic downturn (see Figure 8). Now, almost half (46 percent) believe they have been highly impacted by the downturn, while only a fourth (25 percent) believe the impact on their businesses is low. Thus, as the recession lingers, it has had at least some impact on three out of four small businesses.

Figure 8

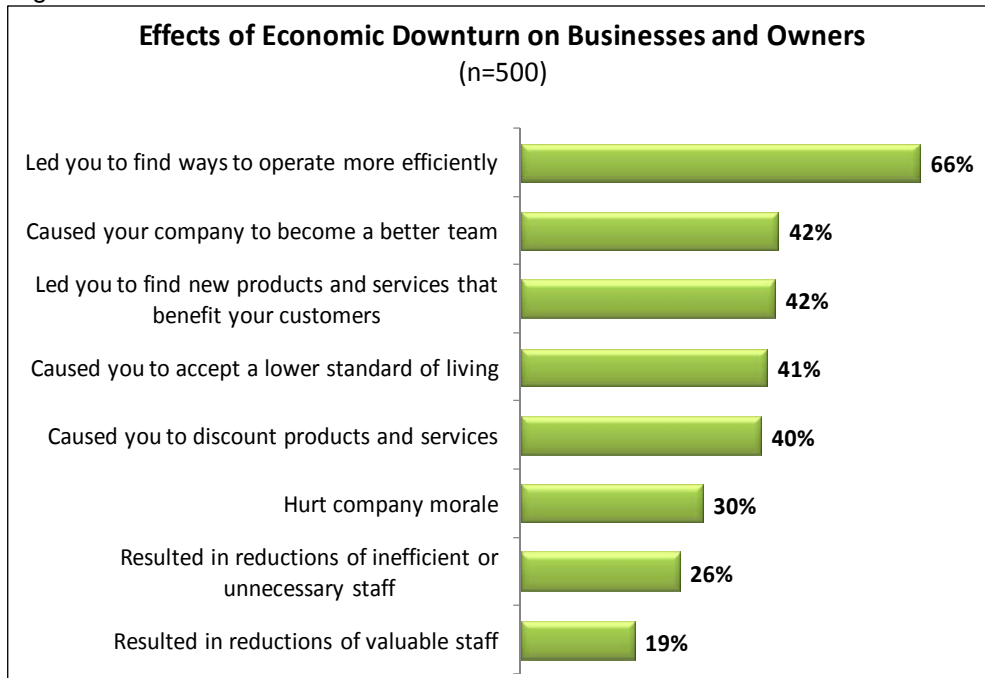


*Note: Non-response not included in sample.

The recession has affected America’s small businesses in many ways, and not all are negative. The most common impact of the economy has been to lead small businesses to find ways to operate more efficiently (66 percent cite this as an outcome of the economy) (see Figure 9). Other positive outcomes of the downturn include becoming a better team, finding new products and services that benefit customers, and reducing inefficient or unnecessary staff. These outcomes will benefit small business in the long run by making them more competitive. They are reducing costs, lowering overhead, and innovating on behalf of the customer. The challenges of the economy are leading the owners and their employees to work together for the future.

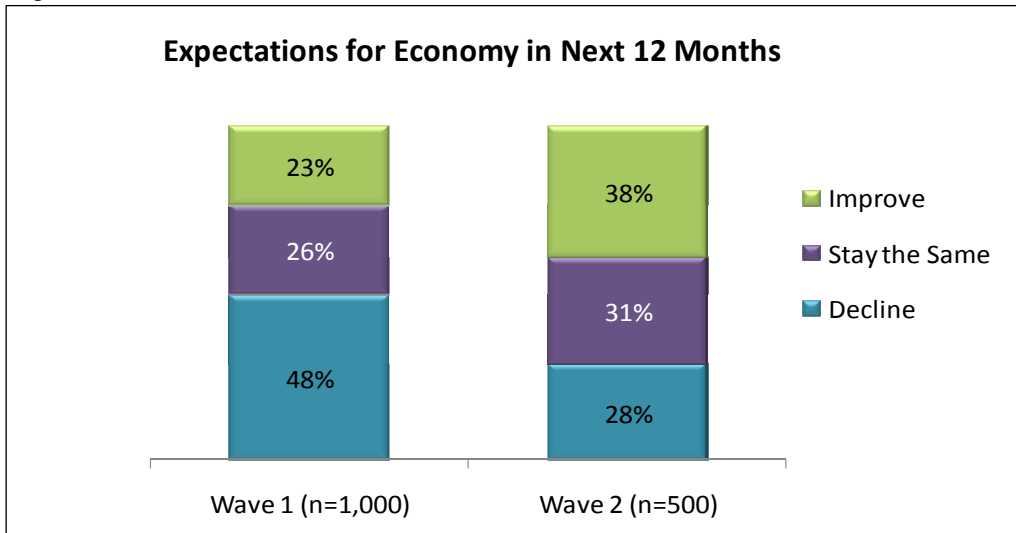
The most serious negative impact of the recession highlights both the suffering and commitment of small businesses in the face of hard times. Two out of five owners (41 percent) have had to accept a lower standard of living. Another 30 percent have found that the recession has hurt company morale and a fifth (19 percent) has had to reduce *valuable* staff.

Figure 9



What do small businesses see for the future? Back in December/January, half (48 percent) of small-business owners expected the economy to decline in the next 12 months, twice as many as those who expected the economy to improve (23 percent) (see Figure 10). Despite the recession’s widespread impact on small businesses, the 12 month outlook has improved to the point that more small-business owners now think the economy will improve (38 percent) than decline (28 percent) in a year. Even so, those who expect things to be better are still in the minority.

Figure 10



A more sobering question is whether small-business owners expect a fundamental shift in their markets once the recession is finished. Few predict an overall reduction in customer spending when the economy improves:

- 44 percent expect their customers to spend at a higher level than before the downturn
- 45 percent expect spending to be at the same level
- Only 8 percent expect spending to be at a lower level.

Although not asked directly in this survey about the reasons for such optimism, one factor may be that small-business owners feel their customers are holding back on spending and will have pent up demand when the recovery begins.

If the economy improves, how will small-business owners invest? Given the fact that small-business owners have used their personal assets to fund their business in the downturn, it is not surprising that the most often cited priority will be to replenish the owners' savings – one out of four (25 percent) owners cite this as their *top* priority. Similarly, another 11 percent will invest in an emergency fund for the business, a way of preventing the need to turn to owner income and savings in the future.

Other top priorities include spending on equipment (19 percent), marketing (13 percent), information technology (8 percent), additional staff (8 percent), and amenities for the owners (7 percent). It appears the major impact that the small business sector will have on the economy when the recovery begins is in spending on infrastructure and marketing. The impact will be dampened by the fact that owners have depleted their assets and reserves to keep their businesses going and will need to rebuild savings rather than invest. As noted earlier, many owners have dipped into savings, cut their pay, borrowed with credit cards and/or taken out home equity loans to finance their businesses. They will no doubt want to avoid this in the future by keeping staffing and overhead low and by ensuring there are sufficient reserves for the next downturn.

About the Small Business Success Survey

The baseline for the Small Business Success Survey was conducted in December 2008 through January 2009. A total of 1,000 small business owners were interviewed by telephone. The second wave reported here was conducted in June 2009 among 500 small-business owners. Small businesses included in the study were privately owned (not publicly traded), for-profit, had fewer than 100 employees, and had a payroll and/or contributed to at least 50% of the owner's household income. The data are weighted to ensure representativeness to the entire population of small businesses in the U.S.

The survey is longitudinal in nature, and will track trends in Small Business Success over time. These are the results from the second wave of data collection.

The survey is sponsored by Network Solutions, LLC and the Center for Excellence in Service at the University of Maryland's Robert H. Smith School of Business. Rockbridge Associates, Inc., an independent marketing research firm, conducted the survey.

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