Small Business: Big Challenge

A Survey of Small Firms in Upstate New York

Buffalo Branch
Federal Reserve Bank of New York
Community Affairs and Regional Economics

In partnership with
Center for Governmental Research Inc.
Rochester, NY • New York, NY

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SUMMARY

In recent years, the contributions of small business to the American economy have become increasingly apparent. Small firms are a significant source of new jobs, and play crucial roles in the development of new technologies and provision of economic opportunities. Small businesses may be especially critical to the regional economies of upstate New York, where a number of large employers have either moved their operations or scaled back their workforces. As a result, it is important to understand the factors that affect small business growth in the region.

Recognizing the growing importance of small firms to the upstate New York economy, the Buffalo Branch of the Federal Reserve Bank of New York in partnership with the Center for Governmental Research (CGR) surveyed small businesses in western and central New York State.[1] Small business owners know first hand the challenges of operating a business in the region, and their insight is vital to comprehending what is necessary for future job growth.

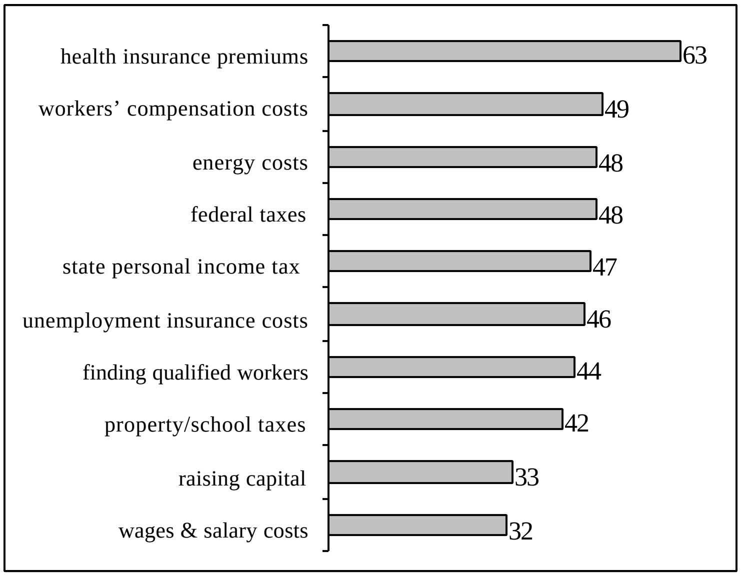
The primary objective of the survey was to identify what small business owners perceive to be the chief barriers to the growth of their companies. The survey also sought to determine the factors that encouraged small businesses to locate in the region, the ways in which new technologies were impacting small firms, and how the opinions of minority, women, and non-minority owners compared. The major findings of the survey were as follows:

Chief Barriers to Growth

Survey results suggest that small businesses in upstate New York face challenges similar to those confronted by small businesses nationwide. The chief concerns cited by respondents were non-wage worker costs, taxes, energy costs, and labor availability.

[1] The Center for Governmental Research is an independent, nonprofit research and management consulting organization based in Rochester, New York.

Chief Reported Barriers to
Small Business Growth in Upstate New York
Percentage of Respondents Identifying Each Barrier as Significant



The Cost of Health Care Is the Number One Concern

The foremost concern among small business owners in upstate New York are health insurance premiums, with 63 percent rating this cost as a significant barrier to growth. The cost of health care is typically cited as the number one concern of small firms nationwide.

Workers’ Compensation and Unemployment Insurance

Workers’ compensation and unemployment insurance appear to be particularly burdensome to upstate New York small businesses. Both of these costs were cited as significant barriers to growth by about half of the respondents, but rank low in nationwide small business surveys.

Taxes, Energy Costs, and Finding Qualified Workers

Taxes, energy costs, and finding qualified workers are also among the top concerns of the region’s small businesses. Federal taxes and the state personal income tax were reported as significant barriers by about half of those surveyed, while property/school taxes were cited as significant by 42 percent.

Other Major Findings on Barriers to Growth

Regulation as a Barrier to Small Business Growth

Our findings suggest that government regulation is not as serious an obstacle to New York State small businesses as is often assumed. Regulatory barriers related to land use, health, and the environment ranked low among the concerns of survey respondents.

Opinions of Minority and Women Small Businesses Owners

Survey results suggest that, for the most part, small business owners face similar challenges regardless of race or gender. Two notable exceptions to this finding were as follows:

- Woman- and minority-owned businesses were more likely to report difficulty in obtaining credit from traditional sources (such as banks and savings associations) than non-minority-owned businesses. Just one-third of non-minority-owned firms noted difficulty with traditional sources of credit, while 41 percent of woman-owned businesses and 50 percent of minority-owned businesses reported difficulty in this area.
- Minority-owned firms appear to be having a more difficult time finding qualified workers than their non-minority- and women-owned counterparts.

Opinions of Firms That Have Considered Moving Out of New York State

Just under one-fourth of small businesses say they have considered leaving New York State in the last three years. These firms, like small businesses generally, ranked health insurance premiums as the most significant barrier to growth. However, the state personal income tax ranked second and finding qualified workers ranked third among firms that have contemplated a move, somewhat higher than these factors ranked among all small businesses in the survey.

Why Firms Are Operating in Upstate New York

When asked to indicate the two main reasons for their current business location, 54 percent of the respondents cited the fact that they or their families were from the area, while 38 percent cited the location's proximity to their customers. This finding reflects the survey's predominance of very small, family-owned businesses that primarily serve local markets. The next most frequently cited reasons for current location were quality-of-life/standard-of-living and low rent/property costs, suggesting two areas in which upstate New York compares favorably with other regions as a location for business.

Technology and Small Business

Survey results demonstrate the importance of new technologies to upstate New York's small businesses. Fifty-four percent of respondents reported that they had recently made a significant investment in technology. Half of the region's small firms are on the Internet, a usage rate similar to that for small firms nationwide. Another 15 percent of surveyed businesses would like to be on the Web, but find it too costly. Our results show no evidence of a digital divide. Minority-owned firms were more likely to have made an investment in new technology than non-minority-owned firms, and Internet use varied little among ownership groups.

What Small Businesses Need

Survey respondents indicated that what they need most to grow their businesses is more demand for their product or service, followed by better access to capital, lower taxes/fees, and lower non-wage labor costs.

Overall, surveyed small business owners are ambivalent about the performance of local educational institutions. Less than a third believe that local schools, colleges, and universities are teaching the skills their companies need.

Finally, upstate New York's small business owners see a need for better access to information about small business resources. Almost three-fourths of the respondents indicated that both a statewide guide to available resources and a small business assistance center would be helpful.

Acknowledgements

We wish to thank the Buffalo Niagara Partnership, Niagara Falls Area Chamber of Commerce, Greater Rochester Metro Chamber of Commerce, and Greater Syracuse Chamber of Commerce for hosting focus group meetings and helping to raise the response rate to this survey. We are also grateful to the small business owners that participated in the focus groups or completed and returned survey questionnaires.

Kent Gardner, Ph.D. of the Center for Governmental Research Inc. consulted on the technical tasks necessary for the successful completion of this survey. We would also like to acknowledge the Community Affairs and Regional Economics staff of the Buffalo Branch, Federal Reserve Bank of New York, which designed and implemented the data collection and analysis and authored this report.

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Chapter 1
INTRODUCTION

In 1997, small businesses with fewer than 100 workers accounted for almost 38 percent of all U.S. employment.[2] Indeed, evidence suggests that small firms now create more *new* jobs than their larger counterparts do.[3] In addition, small businesses appear to play two crucial roles in the American economy: incubators of new ideas that spark technological change and productivity growth, and providers of first-rung access to the mainstream economy for millions of minority, women, and immigrant entrepreneurs.

The ability of small firms to generate jobs takes on added significance in upstate New York, where economic restructuring has resulted in a steep decline in manufacturing employment and slow economic growth. The region can no longer rely on large manufacturing plants to provide thousands of high-paying jobs and undergird its economic base.

Recognizing the growing importance of small firms to the upstate New York economy, the Buffalo Branch of the Federal Reserve Bank of New York in partnership with the Center for Governmental Research (CGR) surveyed small businesses in western and central New York State. Small business owners know first hand the challenges of operating a business in the region, and their insights are vital to understanding what is necessary for future job growth.

Survey Objectives

The primary objective of the survey was to identify what small business owners perceive to be the chief barriers to the growth of their companies. In addition, the survey was designed to accomplish the following secondary objectives:

- Compare the experiences and perceptions of women, minority and non-minority small business owners.

[2] U.S. Bureau of the Census, *1997 Economic Census*, Table 2a.
[3] Zoltan J. Acs, Catherine Armington, and Alicia Robb, *Measures of Job Flow Dynamics in the U.S. Economy*, Small Business Administration, January 1999. According to this report, in 1994-95, small firms with fewer than 500 employees generated 72.7 percent of the 3.59 million new jobs, with the largest growth occurring at microbusinesses with one to four employees.

- Evaluate small business access to credit and capital.
- Ascertain why small business owners have established businesses in upstate New York.
- Assess the application of new technologies and their impact on the region's small firms.

Methodology

In October 2000, a twenty-question survey (see Appendix) was sent to 4,095 upstate New York small businesses. The surveyed businesses were randomly selected from a universe of 88,335 firms located in the Western, Central, and Finger Lakes regions of New York State. This universe included the four metropolitan areas of Buffalo, Jamestown, Rochester, and Syracuse.

The sample of small businesses was stratified by employment size, industry sector, and type of ownership to obtain a sufficient cross-section of firms and to ensure the adequate representation of specific groups. Stratification also allowed an analysis of the impact of barriers on different industry sectors and ownership groups. The sample was divided into five industry sectors: finance, insurance & real estate (FIRE); manufacturing; service; trade; and transportation & communications. The trade sector included both retail and wholesale trade. It is also important to note that the service sector included high-level services that can be traded, such as legal, engineering, and accounting, as well as services that are for local consumption, such as auto repair, dry cleaning, and haircutting. The three ownership groups were non-minority-owned, minority-owned, and women-owned. The table on the following page shows the number of firms in the sample universe by industry sector and ownership group.

The survey prompted respondents to evaluate twenty-four potential barriers to the growth of their companies on a scale of one to seven, with one indicating "not a barrier" and seven indicating a "significant barrier." For the purpose of analysis, we interpreted a barrier to growth to be "significant" if it was given a six or seven. The survey included additional questions designed to fulfill the secondary objectives.

Reported data have been weighted to reflect each group's proportional representation in the general population and to correct for differences in the groups' response rates. Overall, the survey response rate was just under 22 percent. The response rates for each industry sector and ownership group and a further discussion of survey methodology can be found in the Appendix.

Number of Firms in Twenty-county Universe, by Industry and Ownership Group

Industry	No. of firms
Finance, insurance & real estate	7,340
Manufacturing	6,115
Trade	28,079
Transportation & communications	3,632
Service	43,169
Ownership group	
Non-minority-owned	74,797
Minority-owned	2,175
Women-owned	11,536

Report Organization

Chapter 2, Findings, presents and discusses the report findings and is divided into the following four sections:

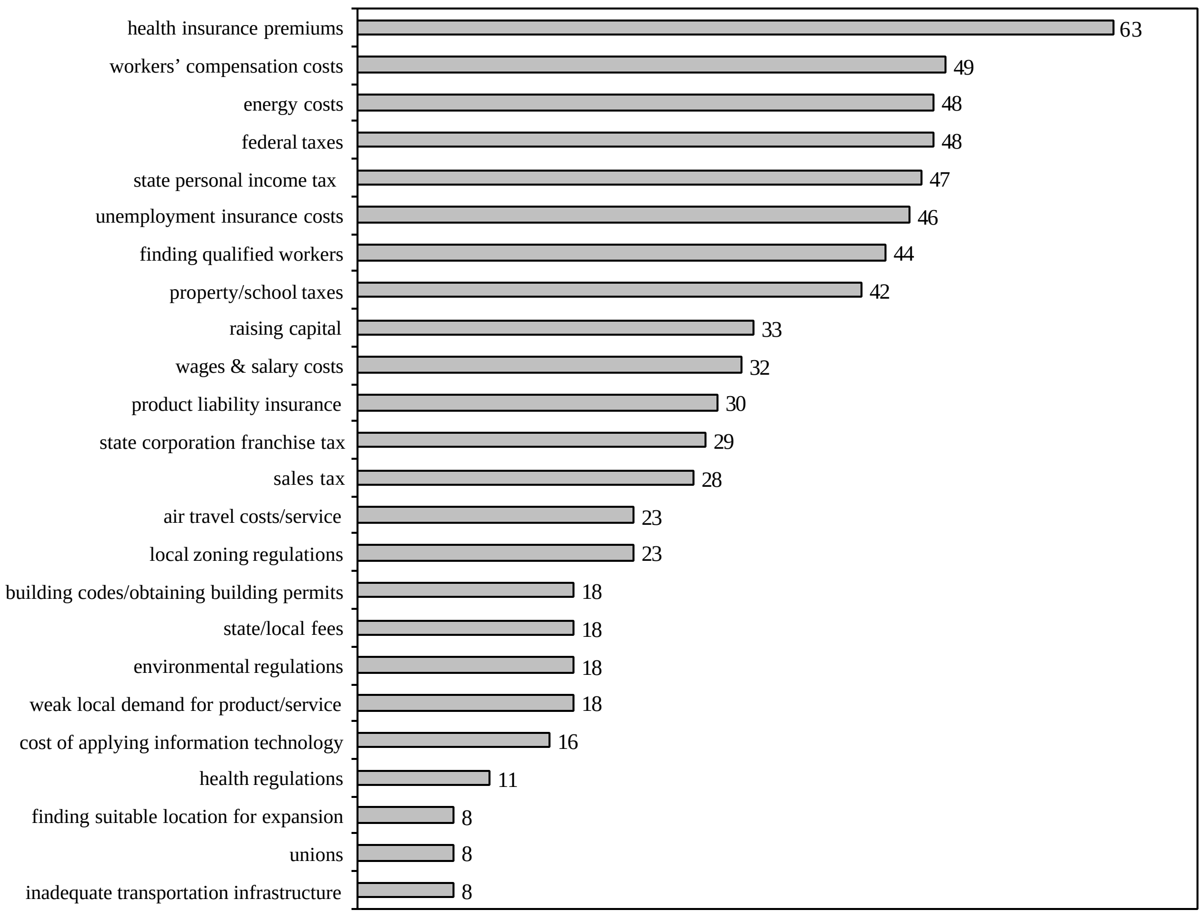
- *Barriers to Growth* discusses results regarding the 24 potential barriers to growth and small business access to credit and capital.
- *Doing Business in Upstate New York* presents findings on small business expansion, relocation, and reasons for current business location.
- *Technology and Small Business* outlines findings on the use of technology and its impact on the region's small firms.
- *What Small Businesses Need* describes owner opinion about local educational institutions, small business resources, and their most pressing needs.

Chapter 3, Conclusion, outlines and briefly summarizes the survey's major findings.

Chapter 2
FINDINGS

Barriers to Growth

Chart 1
Barriers to Small Business Growth in Upstate New York
Percentage of Respondents Identifying Each Barrier as Significant



Chief Concerns of Upstate New York Small Business Owners

The small business owners participating in the survey evaluated twenty-four potential barriers to the growth of their companies. Chart 1 shows the results of that evaluation, ranking each barrier based on the percentage of all respondents that reported it to be significant. The discussion that follows focuses on the top ten concerns.

Non-wage Labor Costs

By far, the foremost concern among small business owners in upstate New York is the cost of health insurance, with 63 percent of the respondents citing health insurance premiums as a significant barrier to growth. Underscoring the breadth of their impact, health insurance premiums were ranked either first or second by every industry and ownership group. The cost of health care has been a huge concern to small businesses nationwide, as indicated by the number one ranking it received in a 2000 survey conducted by the National Federation of Independent Business (NFIB).[4]

Two other non-wage labor costs—workers' compensation and unemployment insurance—also rank among the top concerns of the region's small business owners, with about half of the respondents citing these barriers as significant (Chart 1). While workers' compensation draws frequent criticism as an impediment to business growth in New York State, unemployment insurance garners much less attention. Both workers' compensation and unemployment insurance ranked low in the 2000 NFIB survey, suggesting that these costs are more burdensome for New York State's small firms than they are for small firms nationally. Non-wage labor costs appear to be the most troublesome to transportation & communications firms and trade firms (Table 1). In contrast, service firms demonstrate the least overall concern about non-wage labor costs.

Table 1

Non-wage Labor Costs, by Industry

Percentage of Respondents Identifying Each Cost as a Significant Barrier

	Health insurance premiums	Workers' compensation costs	Unemployment insurance costs
Trade	72	61	58
Transportation & communications	69	74	60
Manufacturing	64	51	46
Service	61	38	38
Finance, insurance & real estate (FIRE)	60	48	43

[4] *2000 Problems and Priorities Survey*. July 2000. National Federation of Independent Business.

Energy Costs

The cost of energy, identified as significant by almost half of those surveyed, also ranks high as a barrier to small business growth (Chart 1). New York State continues to experience high electricity prices, and that fact is likely reflected in the results. However, it is interesting to note that the industries most concerned about energy costs are transportation & communications and trade (Table 2). In this analysis, the transportation & communications sector was dominated by small trucking and other highway transportation companies. Fuel is a major expense for such firms, so the high ranking of energy costs is no surprise. But what may be surprising is the considerable concern about energy costs among trade firms, particularly when compared to manufacturers; overall, manufacturing is more energy intensive than trade. This apparent discrepancy may be due in part to the differential pricing of electricity, whereby the commercial rates that most trade businesses pay tend to be about twice as high as manufacturers' industrial rates.

Table 2

Energy Costs, by Industry

Percentage of Respondents Identifying Energy Costs as a Significant Barrier

Trade	68
Transportation & communications	61
Finance, insurance & real estate (FIRE)	50
Manufacturing	42
Service	37

Taxes

Three kinds of taxes were frequently rated as significant barriers the growth of small businesses (Chart 1). Federal taxes and the state personal income tax were reported as significant by about half of the respondents, while property/school taxes were cited as such by 42 percent. Overall, concern about taxes was most prevalent among transportation & communications firms, while it was least prevalent among manufacturers (Table 3). Property/school taxes, however, were particularly burdensome to FIRE and trade businesses. Overall, property and school taxes appear to be declining in relative importance. In a 1998 survey of New York State small businesses conducted by CGR, property taxes ranked as the greatest barrier to growth, while in this survey they ranked eighth.[5]

Table 3
Taxes, by Industry
Percentage of Respondents Identifying Each Tax as a Significant Barrier

	Federal taxes	State personal income tax	Property/school taxes
Transportation & communications	61	56	51
Trade	49	44	60
Finance, insurance & real estate (FIRE)	49	48	67
Service	48	48	43
Manufacturing	38	39	41

Labor Availability and Cost

At the time of the survey, tight labor markets were making it difficult for many businesses across the U.S. to find workers. Survey results show that—despite slower job growth in upstate New York—the region's small businesses were having trouble locating capable employees as well. Forty-four percent of the respondents cited finding qualified workers as a significant barrier to the growth of their businesses (Chart 1). Manufacturers were the most likely to exhibit concern about a lack of qualified workers, with 55 percent reporting this barrier as significant (Table 4).

Wage and salary costs were a moderate concern among small business owners, with about one-third citing them as a significant barrier to growth (Chart 1). Worry over wage and salary costs varied little among ownership groups and industries, although FIRE firms expressed somewhat less concern about them than small businesses generally (Table 4).

[5] *Barriers to Small Business Growth in New York State: A Barometer of Opinion*. November 1998. Center for Governmental Research.

Table 4
Labor Availability and Cost, by Industry
Percentage of Respondents Identifying Each Barrier as Significant

	Finding qualified workers	Wage & salary costs
Manufacturing	55	28
Transportation & communications	44	36
Trade	44	33
Service	41	33
Finance, insurance & real estate (FIRE)	38	24

Regulation as a Barrier to Small Business Growth

Government regulation is often seen as a hindrance to business growth in New York State, and the costs of regulatory compliance are thought to be especially burdensome to small business. However, potential barriers related to regulation ranked low among the concerns of small businesses participating in the survey (Chart 1). Local zoning regulations were identified as significant barriers by less than a fourth of small businesses, and building codes/obtaining building permits and environmental regulations were reported as significant by less than a fifth of firms. Health regulations were considered a significant barrier by just 11 percent of the respondents.

The generally low ranking of potential barriers related to regulation might in part reflect the fact that specific regulations affect only certain types of businesses. For example, environmental regulations are very important to a dry cleaner or gas station, but of little consequence to a software firm. This fact was underscored to some extent in the survey findings on three regulations related to land development: zoning regulations, building codes, and environmental regulations. FIRE firms, all of which are heavily involved in land development, were the most likely to identify these factors as problematic, with about 30 percent of the respondents in each case indicating that the regulation was a significant barrier to growth.

Minority- and Women-owned Small Businesses

In most instances, minority, women, and non-minority owners reported similar levels of concern about individual barriers to growth. In several areas, however, opinions diverged (Table 5). Minority-owned firms were more likely than non-minority- and women-owned firms to consider two non-wage labor costs—workers' compensation and unemployment insurance—as significant barriers. Minority owners were especially concerned about workers' compensation costs, with almost 70 percent reporting this barrier as significant compared to only about half of women and non-minority owners.

According to the survey, 57 percent of minority owners viewed finding qualified workers as a serious problem, considerably more than the percentage of non-minority and women owners that did. Minority owners were also more likely to perceive energy costs as a significant barrier than the other ownership groups.

Table 5
Barriers to Growth, by Ownership Group
Percentage of Respondents Identifying Each Barrier as Significant

	Workers' compensation costs	Energy costs	Unemployment insurance costs	Finding qualified workers
Minority	69	61	58	57
Non-minority	49	49	46	45
Women	48	41	42	39

Firms That Have Considered Leaving New York State

Close to one-fourth of small businesses reported that they have considered relocating outside of New York State over the past three years. We separate out these firms to identify the factors that they believe are most burdensome. Like small businesses in general, firms that have considered a move cited health insurance premiums as the most significant barrier to growth (Table 6). However, the state personal income tax ranked second and finding qualified workers ranked third, somewhat higher than these potential barriers ranked among all small businesses in the survey.

We also compare the responses of firms that have seriously considered a move to those that have not. Not surprisingly, “movers” were more likely to classify potential barriers as significant than were “non-movers”, indicating that movers are generally more dissatisfied with the business climate. Table 6 shows the specific factors with the widest difference between the two groups.

Table 6

Barriers to Growth, Firms that have Considered Relocating Outside of New York State

Top Five Barriers of Potential Movers	*Barriers in Which Potential Movers and Non-movers Differ Most*
Health insurance premiums	Inadequate transportation infrastructure
State personal income tax	Building codes/obtaining building permits
Finding qualified workers	Weak local demand for product/service
Unemployment insurance costs	Health insurance premiums
Energy costs	State corporation franchise tax

Inadequate transportation infrastructure—not commonly considered a problem in slow growing upstate New York—was much more of a concern to firms that have contemplated relocating than to those that have not (25 percent vs. 1 percent). Building codes and permits (36 percent vs. 12 percent) and weak local demand (32 percent vs. 14 percent) also exhibited a broad variance in opinion between movers and non-movers.

This difference between movers and non-movers may be due in part to the disparate impacts that cost, regulatory and market factors have on different kinds of businesses, coupled with a belief by firms especially hindered by such factors that conditions may be more favorable in other states. For example, the lack of local demand would be a more significant barrier to firms that rely solely or predominately on their local markets than to those that export outside the region. If such firms are sufficiently footloose, they might consider a move to a growing area that has expanding local markets.

Small Business Access to Credit and Capital

One area of particular concern to the Federal Reserve is small business access to credit and capital. One-third of all small business owners in the survey viewed raising capital as a significant barrier to the growth of their firms. We looked at this issue more deeply by measuring the percentage of firms that encountered difficulty when seeking capital from different sources and for different purposes (Table 7).

Table 7

Percentage of Respondents Reporting Difficulty in Accessing Various Types of Financing, by Industry and Ownership Group

	Traditional financing	Venture or angel capital	Technology-related financing	Export financing
All firms	34	50	34	42
Transportation & communications	49	52	31	38
Manufacturing	41	52	42	46
Service	33	59	35	57
Trade	31	43	35	29
Finance, insurance & real estate (FIRE)	25	34	24	28
Minority	50	55	45	43
Women	41	48	45	47
Non-minority	33	50	33	41

Traditional Financing

Of the firms in the survey that had attempted to access traditional financing (for example, from banks and savings associations), over a third reported difficulty. The transportation and communications sector reported the most trouble, with almost half of the owners citing difficulty in obtaining credit from traditional sources. As noted previously in this report, small transportation companies such as truckers, movers and limousine services dominated this sector.

Traditional Financing and Type of Ownership

The survey findings in regards to access to traditional financing show disparity among ownership groups. One-third of non-minority-owned firms noted difficulty in obtaining credit from traditional sources, while 41 percent of woman-owned businesses and 50 percent of minority-owned businesses reported difficulty in this area. These findings are consistent with past studies conducted by the Federal Reserve System.[6]

Venture and Angel Capital[7]

There is a general belief that venture and angel capital are hard to obtain in upstate New York; the survey results support this notion. Over one-half of the surveyed businesses had sought venture or angel capital and 50 percent of those firms reported difficulty. Service firms were the most likely to note problems in obtaining capital from these sources, with almost 60 percent indicating difficulty.

Technology and Export Financing

Discussions held during pre-survey focus groups indicated that the region's small businesses might be having problems obtaining financing for the application of new technologies and for the facilitation of the foreign export of goods and services. We found that almost three-fourths of the respondents had sought technology-related financing, with one-third of those businesses reporting difficulty. While two-thirds of both manufacturing and FIRE firms had recently invested in new technology, findings show that their experiences tended to differ. Manufacturing firms cited difficulty in obtaining technology-related financing most often (42 percent), while FIRE firms were the least likely to report difficulty (24 percent).

A little over a third of the respondents had tried to obtain export financing, with 42 percent of them reporting difficulty. Accessing credit for this purpose was especially hard for service companies, with difficulty indicated by 57 percent of such firms.

[6] For example, three research papers presented at a March 1999 Federal Reserve System conference on business access to capital and credit found that African-American-owned small businesses were less likely than white-owned businesses to receive loans, holding constant a number of other factors likely to account for differences in creditworthiness. However, the researchers differed widely in the extent to which they were prepared to draw conclusions from their findings. All three studies used data from the 1993 National Survey of Small Business Finances.

[7] Venture capital is equity capital made available by individuals for new companies that commercial banks and other traditional lenders consider too risky or unorthodox. Angel capital is venture capital from a single investor.

Technology-related Financing and Type of Ownership

Survey findings suggest that woman- and minority-owned businesses find it more difficult to obtain technology-related financing than non-minority-owned businesses do. While just one-third of non-minority owners reported difficulty in obtaining credit for this purpose, 45 percent of both women and minority owners did.

Impact of Recent Economic Slowdown on Barriers to Growth

At the time small businesses were surveyed, the national economy was nearing its peak in the business cycle. Upstate New York—which had caught up to the U.S. in job growth during the latter part of the 1990s after lagging for much of the decade—was near its peak as well. A year after the survey, the national and upstate New York economies were contracting. We resurveyed the manufacturing firms that had participated in the original study to gain an understanding of how the slowdown might be impacting small businesses.[8] This section highlights the results of the follow-up survey.

Table 8

Barriers to Growth, Impact of Economic Slowdown

Percentage of Manufacturers Identifying Each Barrier as Significant, 2000 and 2001

	Original survey 2000	Follow-up survey 2001
Air travel costs/service	25	3
Finding qualified workers	55	33
Weak local demand for product/service	19	37
Property/school taxes	41	26

Most of the potential barriers to growth drew comparable levels of concern in the original and follow-up surveys, thus indicating that the challenges faced by the region's small businesses—despite the business cycle—remained the same in many respects. Table 8 shows the potential barriers that did exhibit a significant change in owner opinion from 2000 to 2001.

[8] The 152 manufacturing firms that responded to the original survey were sent follow-up questionnaires. Responses were received by 82 of those companies, a response rate of 54 percent.

The greatest shift was seen in the percentage of manufacturers that viewed air travel costs/service as a significant barrier to growth, which went from being a significant concern of a quarter of respondents to barely a concern at all. Part of this decrease might be attributable to lower airfares and improved service in Buffalo, which has seen increased operations by low-cost carriers. Buffalo Niagara Airport directly serves about a third of the businesses in the survey, and possibly serves another third coming from the Rochester area for less expensive airfares. Rochester has experienced decreased prices in some markets over the past year as well. However, air travel nationwide was down about one-third from the fall of 2000 to the fall of 2001, due both to the economic slowdown and the events of September 11. These factors may have made air travel less of a concern to the small businesses participating in the follow-up survey, regardless of cost and service.

By the fall of 2001, finding qualified workers was considered a significant barrier by a much smaller percentage of manufacturing firms than it was in 2000 (33 percent vs. 55 percent). This finding can most likely be attributed directly to the 2001 recession, since many manufacturers had begun to lay off workers or curtail hiring. Manufacturers that were adding jobs at the time of the follow-up survey would have also had an easier time locating capable employees. Property/school taxes also became less of a concern to the region's manufactures over the year between surveys, dropping from 41 percent to 26 percent.

Finally, it is no surprise that overall weakness in the upstate economy resulted in an increase in the percentage of small manufacturers that perceived a lack of local demand as a significant barrier. This increase was the greatest for firms with one to four employees, suggesting that these small manufacturers are generally more dependent on their local markets than firms with five to ninety-nine workers are. Of course, manufacturers in the five to ninety-nine size classification were surely seeing a decline in external markets as well.

Doing Business in Upstate New York

Small Business Expansion and Relocation

Despite the general concern over the factors that inhibit business growth in upstate New York, many small businesses continue to operate and thrive in the region. During the three years prior to the survey, only 23 percent of respondents had considered relocating outside of New York State, while 35 percent had expanded their operations (Table 9). For the most part, responses regarding relocation and expansion by individual industries and ownership groups did not vary significantly from those of firms generally. However, manufacturing firms were more likely to have grown than small businesses overall—with almost half indicating they had done so within the past three years.

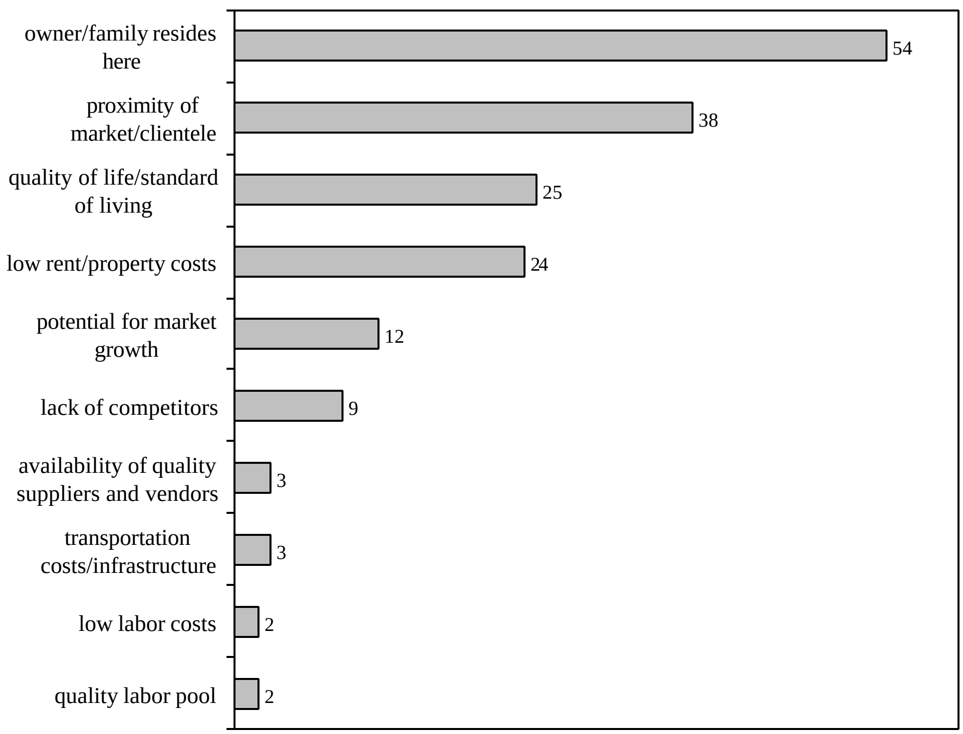
Table 9
Percentage of Small Businesses that have Considered Relocating Outside of New York State vs. Percentage that have Expanded, by Industry and Ownership Group

	Considered relocation in past 3 years	Expanded operations in past 3 years
All firms	23	35
Transportation & communications	30	38
Manufacturing	29	48
Service	25	34
Finance, insurance & real estate (FIRE)	25	38
Trade	16	31
Women	26	28
Minority	25	31
Non-minority	23	37

Reasons for Current Business Location

Chart 2 sheds light on why small businesses in the survey are operating in upstate New York. When asked to cite the two most important reasons for their current business location, 54 percent reported that it is where they and their family reside, while 38 percent cited proximity to their customers. These findings are closely tied to the nature of the very small businesses that dominate the survey. Many of these businesses—such as restaurants, automobile repair shops, and dry cleaners—are homegrown family operations that provide services to their local markets.

Chart 2
Reasons for Current Business Location
Percentage of Respondents Citing Each Reason



The next most frequently cited reasons for current business location were quality-of-life/standard-of-living and low rent/property costs, each cited by a quarter of the respondents. Such indigenous attributes are important to small firms regardless of the type of business. An area's quality-of-life is an important factor in attracting skilled workers—as well as business owners—while the advantage of inexpensive operating space is readily apparent.

Findings regarding the reasons for current business location varied somewhat across industries. Quality-of-life was especially important to service firms, 35 percent of which cited this reason. On the other hand, low property costs were more significant to manufacturers, with this reason cited by 33 percent of such businesses. This difference may be due to the fact that service firms are more likely to value highly-skilled workers (e.g. doctors, lawyers, and engineers), while manufacturing firms are more likely to see production costs as important.

There was also some variation among the opinions of different ownership groups (Table 10). Women owners were considerably more likely than non-minority or minority owners to indicate that they were at their current location because it is where they or their family reside. This may be due to the influence of traditional family responsibilities. On the other hand, minority owners were more likely to cite low property costs as a reason for their current location than the other ownership groups were.

Table 10
Reasons for Current Business Location, By Ownership Group
Percent

	Women	Minority	Non-minority
owner/family resides here	70	44	52
low rent/property costs	16	35	25

Technology and Small Business

The application of knowledge is an increasingly critical factor in firm competitiveness. Innovation can be especially important to small firms, allowing them to compete with their larger counterparts. Firms invest in technology to improve efficiency and reduce costs. Such investments might include the application of information technologies (computers, software, and telecommunications), new manufacturing processes, or improved distribution systems. This section discusses survey results regarding the use of technology by upstate New York's small businesses.

Technology Investment

The survey results demonstrate the importance of new technologies to upstate New York's small businesses, as 54 percent of respondents reported that they had recently made a significant investment in new technology (Table 11). Manufacturing and FIRE firms were the most likely to have invested in technology, with almost two-thirds of the surveyed companies in these sectors indicating they had done so. Perhaps surprisingly, minority-owned firms were more likely to have made such an investment than non-minority-owned firms.

Table 11

Percentage of Small Businesses Reporting a Significant Recent Investment in New Technology, by Industry and Ownership Group

All firms	54
Manufacturing	65
Finance, insurance & real estate (FIRE)	64
Service	53
Transportation & communications	48
Trade	42
Minority	63
Women	58
Non-minority	54

Impact of Technology Investment on Employment

Almost a third of firms that have made recent investments in technology indicated the end result would be an increase in employment, while only 2 percent reported a likely loss of jobs. Almost half of the manufacturing firms anticipated an increase in employment, the highest percentage among industry sectors. But small manufacturers were also the most likely to predict that the application of new technology would result in fewer jobs, with 5 percent indicating a probable decrease in employment.

Internet Use

At the time of the survey, small businesses across the nation were investing heavily in Internet technology. Survey results indicate that upstate's small firms followed this trend, with almost half reporting they were on the Internet (Table 12). This percentage is similar to results from national surveys of small business Internet use.[9]

Table 12
Upstate Small Businesses and the Internet
Percent

	Are you on the Internet?			How has use of the Internet impacted your business?	
	Yes	No, not necessary	No, too costly	Positively	Negatively
All firms	49	36	15	73	4
Manufacturing	62	27	11	69	5
Finance, insurance & real estate (FIRE)	57	28	16	81	4
Service	51	41	8	83	1
Transportation & communications	40	44	15	63	8
Trade	39	36	25	58	10
Non-minority	50	37	15	73	4
Women	48	28	24	72	4
Minority	47	38	15	64	6

[9] For example, a spring 2001 poll conducted by the National Federation of Independent Business found that 57 percent of firms with under 250 employees used the Internet for business related activities.

The industry sector most likely to have made a recent investment in technology was also the most likely to be on the Internet; over three-fifths of small manufacturing firms reported that they were on the Web. Internet use varied little among the three ownership groups, as about half of each group reported that they used the technology.

The small businesses that reported using the Internet generally believe the technology has been beneficial. Three-fourths indicated that the Internet has positively impacted their business, while only 4 percent perceive a negative impact. Trade firms demonstrated the most ambivalence about the contributions of the Web. They had both the lowest percentage of owners who indicated a positive impact and the highest percentage that reported a negative effect. These results may in part reflect the mixed performance of Internet retail. Some small retailers may question whether Internet sales have been worth the investment, while others may feel they have lost business to Web-based retailers. The three ownership groups reported similar Internet usage rates.

The survey also revealed why half the small businesses in the survey were not on the Web. Slightly more than one-third of the respondents did not feel the Internet was essential for their business, while 15 percent reported that applying the technology would be too costly. The perceived importance of technology to manufacturing and FIRE firms was reiterated in this case, as these sectors were the least likely to indicate that the Internet was unnecessary. Despite the greater level of doubt expressed by trade firms about the Web, they were the industry most likely to report that non-usage was due to cost.

Internet Application

Upstate's small firms appear to be using the Internet primarily for the same purposes as Web users generally: e-mail and research. When asked what they used the Internet for, 84 percent of respondents indicated communication and 73 percent indicated research. A significant percentage of the region's small businesses are applying Internet technology more directly in their operations. Almost half of the businesses that are on the Internet are using it for buying and the same proportion are using it for selling, thus joining in the growing trends of business-to-business and business-to-consumer Web interaction.

What Small Businesses Need

Quantifying the perceived barriers to growth is one way to help understand what small businesses need to be successful. Respondents were also asked to specify the one thing that would most improve their company's ability to grow. Most of the responses fell into one of six general categories as shown in table 13.

Table 13
What Small Businesses Need Most to Help Them Grow, by Ownership Group
Percent

	All firms	Non-minority	Minority	Women
More demand for product/service	24	22	30	30
Better access to capital	20	19	27	25
Lower taxes/fees	13	14	8	6
Lower non-wage labor costs	10	11	5	5
More qualified-workers	8	8	15	4
Less government regulation	8	8	3	4

The results paint a somewhat different picture of the factors affecting the region's small businesses than revealed by the ranking of barriers. Categorizing the responses provides a more general sense of the factors that small business owners believe, if changed, would stimulate growth. The number one response among the firms in the survey, cited by 24 percent, is the need for more demand for their product or service. A high proportion of the responses in this category concerned the lack of local demand, with many small business owners citing the need for population or economic growth in their areas. Lack of local demand actually placed low in the individual barrier rankings. This apparent inconsistency may be due to the extreme importance of local demand to some firms, such as those that exclusively serve the local community. Only 14 percent of manufacturing firms cited more demand as their greatest need, suggesting that small manufacturers are less dependent on local markets than are small firms generally.

One-fifth of the survey respondents indicated that better access to capital would best help their businesses to grow, making this the second most frequently mentioned need. Almost half of this group reported a need for more grants or low-interest loans for small businesses. Lower taxes/fees, cited by 13 percent of owners, was the third greatest need among small businesses.

A comparison of greatest need across ownership groups supports findings divulged by the barriers to growth rankings, although the variation in responses are on the border of what is considered statistically significant. Women and minority owners were more likely to cite better access to capital as their most pressing need than their non-minority counterparts. And providing further evidence that they are having exceptional difficulty finding qualified employees, minority owners cited more qualified-workers as their greatest need more often than women and non-minority owners.

Worker Skills and Local Education

As a group, small business owners tend to be dissatisfied with the performance of local educational institutions (Table 14). Forty-five percent of small business owners do not believe that local schools, colleges, and universities are teaching the skills their companies need, while 31 percent believe that they are. Manufacturing firms are the most dissatisfied with school performance; 55 percent indicated that local educational institutions are not teaching required skills, perhaps indicating a lack of math and technical proficiency. FIRE firms are the least displeased with local schools, with only 38 percent of owners registering dissatisfaction. These findings are consistent with other findings in this report, whereby manufacturing firms were the most likely to rank finding qualified workers as a significant barrier, while FIRE firms were the least likely to do so. The ability of each of these sectors to obtain capable employees may be affecting their growth. The FIRE sector has been an important source of jobs in upstate New York, while manufacturing continues to decline.

Interestingly, while among ownership groups minority-owned firms indicated the most difficulty finding qualified employees, they were less likely than woman- or non-minority-owned firms to blame the problem on local schools.

Table 14
Local schools, colleges and universities are teaching the skills my company needs
Percent

	Disagree	Agree
All firms	45	31
Manufacturing	55	21
Service	47	31
Transportation & communications	43	21
Trade	42	33
Finance, insurance & real estate (FIRE)	38	38
Non-minority	45	31
Women	41	31
Minority	41	41

Statewide Resources for Small Business Assistance

Upstate New York's small business community sees value in expanding the level of assistance available to the region's small firms. Over three-fourths of the respondents indicated that a statewide guide listing the resources available to small business would be very helpful. The development of a one-stop center for small business assistance drew similar support, as 70 percent of those surveyed believed that such a facility would be beneficial.

Chapter 3
CONCLUSION

The primary objective of this survey was to identify what small business owners in upstate New York perceive to be the chief barriers to the growth of their companies. The survey also sought to determine the factors that encouraged small businesses to locate and operate in the region, the ways in which new technologies were impacting small firms, and how the opinions of minority, women, and non-minority owners compared. This section highlights the survey's major findings.

Chief Barriers to Growth

The chief barriers to growth cited in upstate New York are similar to those reported by small businesses nationwide: non-wage worker costs, state and federal taxes, energy costs, and finding qualified workers.

According to the survey, the foremost concern among small business owners in upstate New York are health insurance premiums, with 63 percent identifying this cost as a significant barrier to growth. Underscoring the depth and breadth of its impact, the cost of health care was the only barrier to be rated significant by over half the respondents and was ranked either first or second by every industry sector and ownership group. The rising cost of worker health insurance has been a concern of businesses nationwide, and it is clear that many small firms in upstate New York are struggling to keep up with cost increases.

Two non-wage labor costs appear to be particularly burdensome to small businesses in upstate New York: workers' compensation and unemployment insurance. Both of these costs were cited as significant barriers to growth by about half of the respondents, but rank low in nationwide small business surveys.

Taxes, energy costs, and finding qualified workers are also among the top concerns of the region's small businesses. Federal taxes and the state personal income tax were reported as significant barriers by about half of the survey participants, while property/school taxes were cited as significant by 42 percent. The cost of energy was rated as significant by almost half of those surveyed, perhaps reflecting New York State's high electricity prices. Our findings also support evidence of a tight labor market in upstate New York at the time the survey; 44 percent of small businesses cited finding qualified workers as a significant barrier to the growth of their companies.

Regulation as a Barrier to Small Business Growth

Our findings suggest that government regulation is not as serious an obstacle to New York State small businesses as is often assumed. Regulatory barriers related to land use, health, and the environment ranked low among the concerns of survey respondents. The generally small concern expressed over regulation might in part reflect the fact that specific regulations affect only certain types of businesses.

Minority- and Women-Owned Small Businesses

Notwithstanding access to credit and capital (see p. 28), survey results suggest that small business owners face similar challenges regardless of race or gender; in general, the ratings of individual barriers varied little among minority-, women-, and non-minority-owned firms. One exception is the ability to locate capable employees. Minority-owned firms appear to be having more difficulty finding qualified workers than their non-minority and women-owned counterparts. Minority-owned firms were also more likely to cite two non-wage labor costs—workers' compensation and unemployment insurance—as significant barriers.

Firms that have Considered Leaving New York State

Just less than one-fourth of small businesses indicated that they have considered leaving New York State in the last three years. These firms, like small businesses generally, cited health insurance premiums as the most significant barrier to growth. However, the state personal income tax ranked second and finding qualified workers ranked third among firms that have considered a move, somewhat higher than these factors ranked among all small businesses in the survey. In addition, firms that have contemplated leaving New York State demonstrated considerably more concern about several barriers to growth—such as transportation infrastructure, building codes and permits, and weak local demand—than firms that have not considered relocation. This finding suggests that such factors affect businesses differently.

Small Business Access to Credit and Capital

Over a third of the firms that have attempted to obtain traditional financing (for example, from banks and savings associations) and about half of those that have sought angel or venture capital reported difficulty in doing so. Findings in regards to access to traditional financing show disparity among ownership groups. Just one-third of non-minority-owned firms noted difficulty in obtaining credit from traditional sources, compared to 41 percent of woman-owned and 50 percent of minority-owned businesses. These findings are consistent with past studies conducted by the Federal Reserve System.

Impact of the Recent Economic Slowdown on Barriers to Growth

Manufacturing firms participating in the original fall 2000 survey were resurveyed in the fall of 2001 to assess the impact of a slowing economy on upstate New York small businesses. Results of the follow-up survey suggest that, for the most part, the challenges faced by the region's small businesses remained the same. The economic downturn did produce two expected results: an increase in the percentage of small businesses concerned about a lack of local demand, reflecting a decrease in economic activity, and a decrease in those having trouble finding qualified workers, suggesting an easing of the region's labor market.

Small Business Expansion

Over one-third of small businesses have expanded in the last three years. Among industry sectors, manufacturing firms were the most likely to have grown, with almost half expanding during the three year period.

Why Small Businesses Are Operating in Upstate New York

When asked to indicate the two main reasons for their current locations, 54 percent of the respondents cited the fact that they or their families reside in the area, while 38 percent cited the location's proximity to their customers. This finding reflects the high number of survey respondents that are very small, family-owned businesses serving local markets. The next most frequently cited reasons for current business location were quality of life/standard of living and low rent/property costs, suggesting two areas in which upstate New York compares favorably with other regions as a location for business.

Technology and Small Business

Survey results demonstrate the importance of new technologies to upstate New York’s small businesses, as 54 percent of respondents reported they had recently made a significant investment in technology. One of the new technologies that small firms are adopting is the Internet, and our findings indicate that upstate small businesses are keeping up with their counterparts nationwide in this respect. Half of the respondents reported that they are on the Internet, a rate similar to that for all U.S. small firms. Another 15 percent of surveyed businesses would like to be on the Web, but find it too costly. Our results show no evidence of a digital divide among small businesses based on race or gender. Minority-owned firms were more likely to have made an investment in new technology than non-minority-owned firms, and Internet use varied little among ownership groups.

What Small Businesses Need

Survey respondents indicated that what they need most to grow their businesses is more demand for their product or service, followed by better access to capital, lower taxes/fees, and lower non-wage labor costs. In keeping with other findings in the survey, women- and minority-owned firms were more likely to cite better access to capital as their most pressing need than non-minority-owned firms were.

Overall, surveyed small business owners are ambivalent about the performance of local educational institutions. Less than a third believe that local schools, colleges, and universities are teaching the skills their companies need. Interestingly, while minority owners were the ownership group that expressed the most difficulty finding qualified employees, they were the least likely to blame the problem on local schools.

Finally, there is a general belief that, while there is a wide array of resources available to small businesses, owners are often isolated and too busy running their companies to seek help. Survey results suggest that upstate New York's small business owners agree, and see value in facilitating their access to information about such resources. Almost three-fourths of the respondents indicated that both a statewide guide to available resources and a small business assistance center would be helpful.

Appendix

METHODOLOGY

Questionnaire Development

In June 2000, focus groups composed of small business owners from a variety of industries were held in four upstate New York cities: Buffalo, Niagara Falls, Rochester and Syracuse. Opinions were solicited on barriers to growth and other issues related to small business operations to assist in the development of a survey questionnaire.

Sample Universe

The sample universe for this analysis was non-agricultural, non-construction, privately-owned, for-profit businesses with under 100 employees located in the Western, Central, and Finger Lakes regions of New York State. This universe included the four metropolitan areas of Buffalo, Jamestown, Rochester, and Syracuse, and comprised the following twenty counties: Allegany, Cattaraugus, Cayuga, Chautauqua, Cortland, Erie, Genesee, Livingston, Madison, Monroe, Niagara, Onondaga, Ontario, Orleans, Oswego, Seneca, Steuben, Wayne, Wyoming, and Yates.

Stratification

The sample population was stratified to obtain a sufficient cross-section of firms and to ensure the adequate representation of specific groups. Stratification also allowed the comparison of opinions among different industry sectors and ownership groups.

To achieve legitimate stratification for this analysis, the population was first divided into five business sectors as follows:

- finance, insurance & real estate
- manufacturing
- service
- trade (wholesale and retail)
- transportation & communications

The population was further divided into three ownership groups (women-owned/ minority-owned/non-minority-owned), and two size classifications (1 to 4 employees/5 to 99 employees). Business size is based on the entire company rather than individual establishments. So as to draw a representative sample based on business sector, business size, and ownership group, the survey was administered to the following fourteen categories of upstate New York small businesses:

- finance, insurance & real estate, 1-4 employees
- finance, insurance & real estate, 5-99 employees
- manufacturing, 1-4 employees
- manufacturing, 5-99 employees
- service, 1-4 employees
- service, 5-99 employees
- trade, 1-4 employees
- trade, 5-99 employees
- transportation & communications, 1-4 employees
- transportation & communications, 5-99 employees
- minority-owned, 1-4 employees
- minority-owned, 5-99 employees
- women-owned, 1-4 employees
- women-owned, 5-99 employees

Adjustments to Minority- and Women-owned Business Lists and Related Bias

For this analysis, minority-owned businesses were defined as those with African American, Hispanic, Asian, or Native American owners. So that the types of minority- and women-owned businesses matched those in the overall sample, agricultural service and construction firms were purged from the respective mailing lists. The women and minority lists were then supplemented with businesses randomly selected from a list obtained from a Buffalo minority business association (50 women-owned and 100 minority-owned businesses). As a result, results for minority- and women-owned businesses may be slightly biased towards these firms.

Return Rates and Non-response Bias

An average of just under 293 surveys were sent to each of the fourteen categories of upstate New York small businesses, resulting in a total mailing of 4095 surveys. Mailings per category ranged from 272 to 308. A total of 288 questionnaires were returned as “bad addresses,” resulting in a final sample size of 3,797. Of these, 822 businesses completed and returned questionnaires—a response rate of almost 22 percent. Response rates among individual categories ranged from 13 percent for service businesses with 1-4 employees to 33 percent for manufacturers with 5-99 employees. In all business sectors and ownership groups, firms with 5-99 employees had a higher response rate than firms with 1-4 employees. The table below shows the number of returned surveys and response rate by industry sector and ownership group.

Surveys Returned and Response Rates, by Industry and Ownership Group

	Surveys returned	Response rate (percent)
Finance, insurance & real estate	101	20
Manufacturing	152	27
Service	87	17
Trade	119	21
Transportation & communications	111	21
Minority-owned	124	22
Women-owned	128	23

The possibility of bias due to survey response rate bears comment. There is always a concern with mail surveys about potential differences between respondents and non-respondents. The best way to avoid non-response bias is to garner a high response rate. The overall response rate of 22 percent achieved in this case is considered respectable for a mail survey. At the same time, the aforementioned stratification process provided a fairly representative cross-section of upstate small businesses, with none of the categories exhibiting excessively low response rates.

Analysis

Stratification categories were weighted to reflect the actual composition of upstate small businesses. Each category was weighted with a formula that accounted for its actual population in the 20-county upstate New York region, the number of surveys mailed, the number of “bad address” returns, and the total number of returns.

For the purpose of analysis, after categories were weighted the two size categories of each sector were collapsed to form one category. The process resulted in the seven categories shown in the table on the previous page.

An eighth analysis category was created by combining all firms in the five business categories that were neither minority- nor women-owned. This category of non-minority-owned businesses was used for comparisons with minority- and women-owned firms.

Appendix

QUESTIONNAIRE