Small Business: Its Place and Problems
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INTRODUCTION

FROM 1933 to 1944 over 400 bills were introduced in Congress to help small business. The problems of small business are widely discussed. Many efforts have been made to diagnose the difficulties and to prescribe remedies.

All this discussion and effort emphasizes the view that small business is essential to provide commodities and services, to provide jobs and to encourage the great diversity of supplies and services for the benefit of the consumer.

Several million small businesses provide millions of jobs for workers and a living for self-employed owners. Small business is a constant fountain of new ideas, new products and new services. The public as well as big business are more heavily dependent on small business than is commonly recognized.

This Bulletin, which is the work of Dr. Emerson P. Schmidt, economist of the Committee on Economic Policy, analyzes the place of small business in a democracy, shows its contributions in both war and peace, its difficulties, and discusses some of the solutions to its problems.

J. CAMERON THOMSON, Chairman, Committee on Economic Policy

December, 1943

SMALL BUSINESS
Its Place and Problems

ARE MASS PRODUCTION and the supermarket destroying the small independent business unit? Will the demands of efficiency and cost-reduction eliminate the small business in the post-war competitive struggle? Have small businesses secured "their share" of war orders? Does small business have a future? Can the veteran look forward with any confidence to the establishment of a business of his own after the war? In what industries can small business compete effectively? Can and should anything special be done by government for small business?

These are some of the questions which Americans are asking themselves and each other. They are important questions involving not only the future of the individual but the future of American democracy. This bulletin will try to answer some of these questions.

I Why Are These Important Questions?

In the fourth century B.C., Aristotle said:

"The best political community is formed by citizens of the middle class. Those States are likely to be well administered in which the middle class is large, the larger if possible than both the other classes, or at any rate than either singly; for the addition of the middle class turns the scale and prevents either of the extremes from being dominant." (Politics, Book II)
In the 19th century A. D., Lord Acton said:

“All power corrupts and absolute power corrupts absolutely.”

THUS THROUGH THE AGES students of society have generally come to the conclusion that power should be diffused and kept from being concentrated. Small business, if kept healthy, prosperous, and expanding, is likely to encourage this diffusion of power, avoid its concentration and build a strong middle class.

In 1862, Congress passed the Homestead Act under which a typical American philosophy was given expression. Under the law, any one could secure, virtually free of charge, 160 acres of land out of which he could carve his own home and make his living. Instead of allowing the land to fall into the hands of a few large landlords or plantation owners, the purpose was to divide up the great heritage which was ours. As a result, we have today six million farms, owned by an equal number of persons or families. Millions of farmers are owners of livestock, machinery and land. Farming in the United States is small business for the most part. While one-third of the farms are tenant-operated, many tenant farmers of today will be owners tomorrow.

A generation later, in 1890, Congress passed the Sherman Antitrust Law, which stated, “Every contract, combination ... or conspiracy, in restraint of trade or commerce ... is hereby declared to be illegal ... every person who shall monopolize or attempt to monopolize ... trade or commerce ... shall be deemed guilty ... .” Here was another attempt to avoid monopoly, to give the small unit an opportunity to originate, to survive and to grow.

If Aristotle and Lord Acton were right and if American anti-monopoly policy as to both agriculture and other industries was right, it does not require much imagination to see why the foregoing questions about small business are important. For both economic and political reasons, we should be concerned about the growth and survival of small business. This does not mean, however, that we must oppose big business or large-scale operations just because of their size. If a large business is more efficient, can give a better product or service for less money, it has its place in our economy. The efficiency of our great railroad systems, our large steel and other companies, are good examples. They are essential in time of peace, as in time of war, for the sake of a high standard of living and for the sake of national security.

II What is Small Business?

THE AVERAGE MAN, when he uses the term “small business,” probably means almost any type of business locally owned and operated in which the owner is the “boss” and actually is in charge of operations; he may be in business by himself or he may have a few employees with him.

No doubt, in the mind of the average man, the following would qualify as small business: a family-operated farm, the local bank, a grocery or drug store with half-a-dozen employees, a machine shop or manufacturing establishment with one or two dozen employees. A person reared in a large city and accustomed to larger stores and factories would probably include somewhat larger establishments in his conception of small business. A factory with
100 employees in Chicago might be regarded as "small business" but in a town of 2,000 population it would be regarded as "big business".

The Bureau of Foreign and Domestic Commerce has defined small business to include the following: manufacturing plants with 100 employees or less; wholesale establishments with less than $200,000 annual net sales; retail stores, service establishments, hotels, places of amusement and construction companies, with annual net sales or receipts of less than $50,000. Obviously, these definitions are rigid and arbitrary but if comparisons with other countries or other times are to be made, we must have some benchmark. Therefore, in the following discussion, when the phrase "small business" is used it will be used in the sense in which the Bureau defines the term, unless otherwise indicated.

III The Role of Small Business

An industrial civilization such as that of the United States embraces several millions of distinct and separate businesses producing hundreds of thousands of different products and providing many thousands of different services. In 1939, we had 6 million farmers in business. In addition, we had 3 million establishments in manufacturing, distribution and in the various service establishments as shown by the accompanying tabulation.

This table shows that over 92% of our business establishments were classified as small business, indicating the fallacy of the notion held by some people that the man...
with a little capital has no place in our society. It shows that, not including agriculture, we had 3 million separate establishments in business. This means that for every 44 people in the country we had one business concern. It means that for every 15 people at work we had one business establishment and thus about every 15th man has a chance to run his own business.

We commonly think of manufacturing as the place where little business does not have a chance. Yet these figures show that nearly 169,000 concerns or 92% of all manufacturing concerns had 100 employees or less. The table would suggest that in service establishments the man with small capital has the best chance, because here nearly 99% of all businesses are classed as small. Over a million and a half small retail establishments were in existence.

About 45% of the employees of the foregoing 3 million establishments were working for small business. Even in manufacturing, 30% of the workers made their living in small factories, that is, in plants with 100 employees or less.

The small concerns, although constituting over 90% of all concerns and employing about 45% of the workers, are responsible for only 34% of the value of the products or services turned out. In the case of manufacturing, about 30% of the product comes from small plants; in the case of retailing, the small establishments are responsible for about 42% of the sales and in the case of service establishments, the figure is 66%.

From 1909 to 1939, population increased by 44% while the number of manufacturing establishments increased 7%. Thus the number of establishments did not expand in proportion to population growth, but the number did expand. In this same period, the value of the product of small business increased 2.3 times although the value of product of large business increased 3.3 times. Thus it seems that in this 30-year period small business has grown in both numbers and value of output, although its share of total business has been shrinking. In other words, opportunities for small business have increased.

In 1939, 92% of all stores were independent and only 7% were chain stores, although the latter did about 22% of the total volume of business. In 1919, chain stores did 4% of the business and the expansion continued rapidly until it reached a figure of 25% in 1933. Since that time, the proportion of business done by chains has shown a slight decline, standing at about 22% in 1939.

Of the 184,230 manufacturing establishments in 1939, 8,300 were one-man affairs; that is, they had no employees, the owner working by himself—small machine shops, broom factories, cigar factories, etc.—examples of individual enterprise. These businessmen carry on the functions of labor, management, salesman—all by the same person. Some of them probably were just getting started when the census was taken. Some may fail or merge with other businesses. Some will grow to be larger concerns in subsequent years.

Nearly 76,000 manufacturing concerns had from 1 to 5 employees each, while another 49,000 had from 6 to 20 workers. Only 176 establishments had over 2,500 employees. Thus it is obvious that big business has not eliminated the small companies.
The Effect of the War On Small Business

Newspaper headlines and radio announcements have given the impression at times that the war has been especially hard on small business which, if true, might mean that competition in the post-war world would give the consumer less protection and that the man with small capital would have a more difficult time. Thus we are told that hundreds of small retailers have closed up; thousands of filling stations are closed for the duration; 100 large concerns have secured 70% of all war contracts. What are the facts?

First, it should be pointed out that, even in normal times, several hundred thousand businesses discontinue operations every year while about an equal number start up in business, as may be seen by the accompanying data.* During depressions, the “death” rate exceeds the “birth” rate.

The Department of Commerce made a special study to find out what happened to business during the war. Of the nearly 1.6 million concerns with one or more employees in 1939-42,** 272,700 were either liquidated or transferred some time in the period 1940 to 1942. Thus 17.5% of these concerns were no longer in business at some time in the subsequent three years while, of course, some other new ones were established. This figure does not differ radically from what would be expected to happen in a normal peacetime period so that it does not appear that the war has been exceptionally severe on business in terms of survival. Significant, however, is the low rate of business births during the war.

New businesses generally begin small and the discontinuance rate is always highest among small concerns—partly because they are new and have not yet become firmly established. The following figures tell the discontinuance story by size of firm.

<table>
<thead>
<tr>
<th>Number</th>
<th>Percentage</th>
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<tbody>
<tr>
<td>1-3 employees</td>
<td>180,466</td>
</tr>
<tr>
<td>4-7 “</td>
<td>34,120</td>
</tr>
<tr>
<td>8-19 “</td>
<td>20,254</td>
</tr>
<tr>
<td>20-49 “</td>
<td>7,992</td>
</tr>
<tr>
<td>50 or more employees</td>
<td>3,566</td>
</tr>
<tr>
<td>All groups</td>
<td>272,700</td>
</tr>
</tbody>
</table>

* Source: Dun & Bradstreet release; Vital Statistics of Industry and Commerce.
** That is, concerns without employees were ignored because the data were taken from the files of the Old Age and Survivors Insurance records which obviously include only concerns which had employees.

This table shows that 22% of the smallest concerns in operation sometime in 1939-1942 were no longer in operation at some time in 1940, 1941 or 1942. In the case of concerns with 4 to 19 employees, the mortality rate was
not quite so high but, still, one in seven disappeared. However as pointed out above, this rate of disappearance is not greatly different from what happens in normal times so that it appears that the war has not made it unduly hard for business concerns to survive. As mentioned, the war has made it difficult to establish new enterprises.

In the mining industry and in the classification known as Hotels, Amusements and Other Services, about 2 out of every 5 businesses in operation in 1939-1942 disappeared some time in 1940-1942. In manufacturing, the figure was only 16% and in retailing it was just under 10%, although in the latter case about 60,000 stores with one or more employees closed up.

These figures do not tell the whole story for two reasons: (1) they cover only concerns which had employees and do not take account of what happened among the hundreds of thousands of establishments which had no employees—such, for example, as the "papa and mama" stores; (2) while many concerns disappeared, many people found opportunities by opening new establishments, as is evidenced by the fact that in 1941, for example, 329,000 concerns were established. Also, many establishments closed up voluntarily because their owners could secure high-paying jobs in war industries.

By the middle of 1943, there were about 2% more businesses in existence than in 1935, but about 8% less than just before Pearl Harbor.

The Department of Commerce made a special study to discover the effect of the war on smaller manufacturing plants (1 to 125 workers) and to find ways and means of using small plants more effectively. It found that the group of smallest concerns in 1943 experienced a decline in dollar output and in number of employees since 1941; firms with 8 to 20 employees in 1943 held their own in dollar output but experienced a reduction in number of employees, while firms with 21 to 125 employees experienced an increase in both dollar volume and in number of employees since 1941. Only about 4% of the companies were believed to be suffering because of inability to get war orders.

Many thousands of small businesses closed in 1942 and 1943 because their owners found war-industry jobs where their earnings were substantially better than if they had continued in business. So the mortality figures, while far from serious, probably overemphasize the hardships of small business. When the war is over, many of these former businessmen may again open their mines, shops and stores.

It is true that the government has concentrated its war orders very heavily with the 100 largest companies. Nevertheless, every effort has been made to induce these large firms to subcontract business to outside producers. Even without any such encouragement, most of the large companies would have sublet many contracts merely to get on with war production.

V Subcontracting and Small Business

The National Association of Manufacturers made a survey of 190 of the 252 companies which held most of the war supply and equipment contracts during 1942. The 190 companies reported contracts for war materials and supplies during the calendar year 1942 with an aggregate value of $26.2 billions: Of this amount, they re-
ported $13.5 billions distributed to other companies. This is 51% of the total war business of the 190 companies for 1942.

These companies reported that they did business with subcontractors, vendors and suppliers in all of the 48 States. The number of subcontractors, vendors and suppliers totaled 140,424 but this figure contains duplications since numerous concerns held subcontracts from several of the 190 prime contractors.

Duncan W. Fraser, President of the American Locomotive Company, said—"Without the more than 500 subcontractors, suppliers and the thousands of men and women in garages, machine shops and small manufacturing plants we could not have done our part of the job. . . . The majority of our subcontractors and suppliers are small shops—many of them with five to 15 workers and most of them with less than 200."

The Douglas Aircraft Company has awarded subcontracts of all types involving approximately $275,000,000. These awards are spread among some 300 principal subcontractors, and at least 1,500 lesser subcontractors. In one case, a subcontract had been placed for a valve involving 20 different parts. This single subcontractor had in turn brought in seven additional subcontractors to participate in its manufacture. . . . Douglas has extended the scope of its purchases of materials, tools, and equipment, enabling some 8,000 suppliers in 48 States to help furnish the things that make airplanes.

In 1942 General Electric Company utilized services of some 1,400 other companies on subcontracts, which indicates the extensive use certain large corporations have made of subcontractors.

A recent General Motors survey revealed that the 37 manufacturing divisions and operating units of that corporation employ 18,375 different sources for parts and material. Among the GM suppliers, 74% were firms employing less than 500 persons and 58% of these firms had less than 100 employees.

Pontiac Motor Division of General Motors made an aerial torpedo with 5,112 parts; 110 parts were made by Pontiac, 3 parts by other GM divisions and 4,999, or 98%, by outside subcontractors.

Oldsmobile Division of General Motors made a 37-mm aircraft cannon with 267 parts; 3 parts (1%) by Olds, 264 parts (99%) by subcontractors.

Fisher Body Tank Arsenal made the M-4 medium tank with 3,719 parts; 392 by Fisher Body, 1,103 parts by other GM divisions, 2,224 parts (60%) by outside companies.

A Chrysler survey showed 8,079 individual subcontractors. These subcontractors were located in 856 cities in 39 States. Fifty-nine per cent of them were relatively small business concerns, 19 per cent medium-sized, and 22 per cent large organizations. Subcontractors furnished 60 per cent of the 32,703 parts going into 21 major war products of the Chrysler Corporation. In the M-4 medium tank, 72 per cent of the 4,587 parts come from outside sources. Of the 11,542 parts making up a Martin B-26 bomber fuselage, 5,881, or 51%, were manufactured for Chrysler by outside companies. The Dodge 4 x 4 military truck contains 526 Dodge-made parts but 1,127 parts, or 68%, come from suppliers.

The Smaller War Plants Corporation was created by an act of Congress with the purpose of helping small business secure war contracts. It was given authority to enter into, and to place, war contracts; it could become a prime contractor and parcel out parts to subcontractors; it could also give contracts to big companies if it felt that
such action would help the smaller plants. It was also authorized to extend loans to help finance small plants where it was found necessary to do so. At first the SWPC devoted its efforts to encouraging prime contractors to do more subcontracting with small plants; more recently it has taken a more positive approach and has entered into prime contracts itself and subcontracted them to small companies. It has had a measure of success, although it has had to overcome some reluctance on the part of procurement agencies to do business with it.

The foregoing represents the best statistical evidence we have of the impact of the war upon small business. One hears of dozens of small companies which have an honest grievance. Not all has been done that might have been done, especially if more time had been available to spread the war contracts. But, on the whole, the picture is not the dark one sometimes painted.

Of course, the real test will come in the post-war. When peace comes, thousands of war contracts will be cancelled, production will stop and all sizes of companies will have on hand an estimated $75 billion in war contracts. These will be in varying stages of completion; the companies will have billions of dollars invested in raw materials, partly finished goods and finished products.

Every effort is being made by such organizations as the Chamber of Commerce of the United States to encourage prompt settlement of all claims which these companies will have against the government so that they will have the necessary cash to convert to peacetime operation and settle promptly with their smaller subcontractors. The smaller companies may not have adequate reconversion reserves and will require favorable conditions so as to get peacetime raw materials in order to get back into competitive production. This is a serious problem and should receive intelligent attention by government and all responsible citizens.

VI Economic Importance Of Small Business

One of the great values of a free society is what is called free consumer choice. This means that the consumer is not told what he may buy but he can indulge his varying tastes. The rich and the poor, the young and the old, the educated and uneducated, the farmer, craftsman, professional man and businessman—each can buy according to his means and his tastes. Unquestionably, one of the great and enduring values of a free society is the enormous range of commodities and services available to the consumer. If we had only a few large companies bent on efficiency and mass production, there can be no question but that the range of goods and services made available would be reduced. Having a great variety of producers in competition with one another, the tendency for commodities and services to multiply in number, design and quality is truly great.

With nearly 200,000 different manufacturers and the hundreds of thousands of service establishments each competing for the market, progress is almost inevitable. Under the stress of competition, prices tend to be lowered, quality tends to improve, and in order to penetrate the market each producer endeavors to give high value for the money.

Out of this multitudinous effort come new ideas, new
products, improved raw material and better service. An official of General Motors Corporation stated that if his company had a monopoly of the production of automobiles, there would be fewer cars produced within ten years than at the time he made the statement. Monopolies tend to be restrictive and high-price-minded. By having a host of small businessmen, each striving to get ahead and many succeeding, the opportunity for any one business to attain a monopoly is greatly reduced or eliminated. Each acts as a spur to the others. The small business of today may become the large business of tomorrow.

However, we should not attempt to keep alive all businesses. Freedom and democracy imply the freedom to take a chance, to succeed and, indeed, to fail. A free society provides freedom of opportunity but does not guarantee success to all who enter. Success depends primarily on management ability, although, in practice, luck or chance factors often play a role in the outcome.

The small business is the economic seed bed from which rise the majority of new ideas, new methods and the inventions of the Nation. The United States Patent Office records reveal that of all the patents issued between 1921 and 1938, 43% went to individuals and 34.5% to 17,500 small and medium-sized enterprises. In other words, individuals, small and medium concerns accounted for about 77% of all patents issued within this period. Clearly, from an economic viewpoint, the small business and the enterprise of the individual are of the highest importance to our well-being. Mr. F. B. Jewett, president of the Bell Laboratories, Inc., stated—

"Fundamental patents which mark big changes in the arts are more likely to come from the outside than from the inside. I think, in the majority of cases, the chances are ten to one that the fundamental idea will come from outside the big laboratories."

We do not want to minimize the truly great achievement of our great motor car, electric, chemical and other companies, because all of them have large, flourishing laboratories constantly bringing out new products, making improvements, finding new uses for raw materials and making a great contribution to our welfare. Nevertheless, in trying to think of the place of small business in our economy, it is important to recognize that the small business—while frequently less efficient than the large business—does make a great contribution, partly because there are so many of these small units. Many of them barely hang on, others disappear; but out of the great number striving to get ahead, there is a sizable fraction which constantly brings forth new ideas, new products and new methods. In short, there is a definite and useful place for both large and small business in a free economy.

A director of a large manufacturer of railroad cars stated that the war has shown him how utterly dependent upon small business his company is for the supply of numerous small parts which it would not pay the company to manufacture itself. No refrigerator manufacturer and no radio manufacturer, for example, produces all the parts which go into the final product. Rather, they rely on a host of small plants each of which specializes in the making of one or more small parts. The small plant, by catering to the needs of a host of other manufacturers, is enabled to obtain a volume of production which cuts its costs below the costs of the manufacturers if each of the latter tried to make all the essential parts for the final product.

Another great advantage of having many businesses
in a community is that then the community has many employers. This means that the worker has open to him numerous employment offers. If he does not like the policy of one employer or crosses swords with his foreman or plant superintendent, he can secure a job elsewhere. If our policies encourage competition and the establishment of many small employers, this opens up many new employment offers. No one is restricted and opportunities are multiplied.

VII Political and Social Importance Of Small Business

ONE OF THE PRIME ESSENTIALS of a democracy is the equality of opportunity. We have urged the young men to go West. We have provided universal and free education. The young man just out of school should have the opportunity to carve out for himself a place in the economic life of the community. If business were confined to a few large companies in every community, the opportunities for self-employment, self-direction and self-realization would be greatly reduced. The man with ideas, ambition and small capital would not have an opportunity to use his capital, try out his ideas and satisfy his ambition.

Hitler, in his rise to power, made vast promises to the ambitious youth of the land. He knew their longings and promised to fulfill them. For example, he promised to break up the large department stores and provide thousands of opportunities for the rise of small stores—a promise never fulfilled. Many of them had felt frustrated and supported Hitler because of the promises he made for individual opportunity. If we are to avoid having some demagogue appeal to our youth to serve his own rise to power, we must be certain that opportunities are open. Therefore, small business has a fundamental place in a liberal democracy.

By and large, it is the combined effect of the numerous small businesses in the local community which make that community. The payrolls and other earnings of the many enterprises support the schools, the churches, the government services, the recreational and cultural activities of the community. If these businesses are not prosperous the schools will be inadequately financed, the churches will languish and other desirable community activities will be dulled and unstimulating. Flourishing small businesses activate the life, the thinking, the recreational and cultural interests of the people in the community. A multitude of small businesses in manufacturing, service and distribution lend color and variety to the community.

Our taxation and other governmental policies must be constantly reviewed to see whether they bear unduly heavily upon business and discourage the opening of new businesses by the man with ideas, ambition and small capital. This is of the greatest importance and will be one of our most significant post-war problems because, since 1929, our birth and survival rates of new businesses have not been high enough to absorb all of our labor into productive employment.
VIII  New Investment Required To Create Jobs

Ours is a Capitalistic Society; it requires approximately $5,000 investment, on the average, in plant, tools, office buildings and other equipment, etc., to put one man to work. In railroad transportation, it requires $25,000, in steel about the same figure, in manufacturing as a whole about $6,300, in retailing about $5,000. Our labor supply is increasing at the rate of about 700,000 (net) young workers each year, after allowing for those who die, retire or quit.

If we are to prevent mass unemployment and provide jobs for our young people who, for the first time, enter the labor market each year, we must have a high rate of new investment in job-creating facilities. If we establish firmly a large number of new businesses year after year, this is the best assurance that a plentiful supply of new job opportunities are created. American democracy must continue as a living, vital, reality by opening new opportunities for jobs and for business. Without a steady growth of new businesses and new employers, we are not likely to have adequate job opportunities. We must govern our policies so that we place a premium on the man who makes his living by giving jobs. This is important for the post-war. An employer is one who provides employment; we should encourage him and give him an honored place in our democracy.

IX  Limitations and Difficulties Of Small Business

Small business is in competition with large-scale business. Contrary to some popular impressions, mass production and large-scale operations are not of recent origin. In 1776, Adam Smith, the founder of economics, wrote a book entitled “The Wealth of Nations,” the opening chapter of which described the operations of a large pin factory. He pointed out how the work was divided so that each worker performed a single minute operation. In this way, specialized tools were utilized and each worker became highly proficient in his specialty. Instead of the worker passing from operation to operation, picking up and laying down tools, no time was wasted in this “mass production” factory—skills were fully utilized continuously, as was true of each tool. The trend toward mechanization and large-scale operations has continued.

Within limits, it is true that the larger the business or the greater the volume, the more practical it is to subdivide the work and get the advantages of mass production. Small-scale concerns may be able to subdivide work somewhat but rarely to the degree possible in larger operations. This limitation applies not merely to plant operations but also to management, sales, advertising, purchasing, legal, engineering and other aspects of the operation. A large plant can hire, for example, the services of a full-time engineer or attorney, who becomes thoroughly familiar with all the problems and operations. A smaller concern probably hires this talent as it needs it and, therefore, probably does not secure as effective service. A large concern has expert accountants, financial managers, buyers, etc.
In a smaller concern, the general manager may have to perform, or at least closely supervise, all these aspects. He is less likely to be a specialist and a small concern is apt to suffer from the difficulties embodied in the adage, "Jack of all trades and master of none." Of course, for many small concerns this is an exaggeration because many of them are very efficient.

A large filling station, to use a familiar example, with a dozen employees, can hire persons for specific purposes: handling the gasoline pumps, lubrication, washing, tire repair, etc. Each person becomes thoroughly familiar with the tools he uses, the peculiarities of the customers with respect to each service and, if the volume of business is large, he can work at his specialized tasks continuously and efficiently. In smaller stations, one or two persons must constantly shift from task to task, much time is wasted, and they may never develop the proficiency of the workers in the larger establishment.

What has been said about the filling station may apply to other businesses. So we must recognize that "smallness" has its limitations.

Large size brings a technical advantage. If we compare the building and equipment of two companies producing identical products, one of which turns out 1,000 units per week and another turns out 500 per week, we will find that the investment in plant and equipment of the large producer is not twice as large as that of the smaller producer. If each needs an engine for power, let us say 1,000 horsepower and 500 horsepower, respectively, it will be found that the big engine does not contain twice as much steel, copper, and other metals as the smaller engine. Thus, the large producer gets his power equipment cheaper per unit of output than does the smaller producer. Similarly, both producers may have a plant covering an area of 1,000 square feet, but the large producer has four stories to his building, while the smaller company has two stories; yet, the same sized roof will cover both buildings. A quart metal container does not contain twice as much metal as a pint container. In short, size brings a host of engineering economies which are not possible to the smaller concern. These are technical handicaps which may have to be overcome by all other means open to the small company.

The greatest handicap of small manufacturers lies not primarily in physical production but in marketing, advertising and salesmanship. A producer with a volume sufficient to warrant the use of national advertising, the development of a nation-wide sales force, and establishment of his own dealer and retail outlets has an enormous advantage over the producer who must rely on inferior advertising media, on wholesalers and retailers who also handle the lines of his competitors and who in general, because of the smallness of the enterprise, cannot make a continuous, widespread and forceful impression on the buyer. The mail order houses and the chain stores, while at times thought of as injurious to the small business, nevertheless do provide outlets for the product of thousands of small producers who, because of the existence of these large distributors, do not need an elaborate selling organization. In a number of cases small producers have combined in establishing common sales organizations and cooperating in sales efforts in other respects. These techniques merit further study and exploration.

Nevertheless, we all know that small filling stations do survive in competition with large ones. We all know that the small store continues to meet its customers' needs even though a few blocks away a supermarket may be in operation. All this suggests that under a modern society
many factors govern the origin and survival of business units. Matters of location, convenience, the personality of the owner and employees, the ability to cater to special needs—all these help to explain the existence of many, many small businesses.

In some instances the small concern, in closer touch with its employees and customers, is able to improve its own operations and its service. Small business, although finding it difficult to comply with rules and regulations imposed from without, is able to change, to adapt itself to new conditions and to enter new or unusual lines because, being small, this smallness offers a high degree of flexibility.

A large organization with branches, sales offices and other connections all over the country is much more likely to follow a given policy once it is adopted. Small business, with its relatively light overhead costs and its ability to experiment on a small local scale, frequently has an advantage over a larger unit. It is this ability to experiment, to adapt itself and to change which makes small business so important in the economy as a whole.

Furthermore, while large size brings advantages, it also has its disadvantages. Once an establishment grows beyond a certain size, the relations between management and employees may become less personal and morale may suffer. Wastes may go undetected; inefficiencies in the handling of materials, due to lack of adequate supervision, may more than offset the gains from specialization of labor. Indeed, these factors are the chief explanation why the biggest companies do not keep on growing indefinitely large and absorb the whole market.

Moreover, mass production is adaptable only to a limited number of products and generally not at all to service enterprises. For example, the entire consuming public may be willing to buy only 100 copies of a particular hat, or dress or display case. Many service trades and manufacturers cater to specific needs and this may require custom-built products and specialized services. In these cases, large-scale operations are poorly adapted to meet individual needs and the small business has a special opportunity.

While a larger proportion of all business is being done by large concerns, there is no evidence that small concerns will disappear from the scene except perhaps in a few industries, such as manufacturing steel and automobiles. But, even here, we cannot be certain. For example, while three motor car producers make more than 80% of all cars, each of these producers relies upon hundreds of suppliers or subcontractors to make parts. In turn, each large producer relies on thousands of wholesalers and retailers to help in disposing of the product.

Can Small Business Be Helped?

America has never been short of people who wanted to establish their own business—indeed, the desire to be one's own boss, to be in business for oneself, is almost universal. Given favorable conditions such as during a period of prosperity, the birth rate of new businesses rises substantially. But the number of failures during such periods rises almost as rapidly.

This suggests that small businesses in their competitive struggles are themselves in part responsible for the difficulties of survival. If this is true, serious question arises
as to what can be done especially for them by private or governmental effort. That is, if some governmental agency provides special services to enable small businesses to originate and grow—would not the resultant increase in the number of businesses, each trying to get its share of the available business volume, leave the situation just about where it was before the effort to help them was made?

To put the matter in another way: By giving each small businessman better advice, better management tools, tax rebates or other special or regular advantages—while all these aids may reduce costs and raise efficiency—they also tend under competition to reduce prices and thus may tend to leave the various competitors in about the same relative positions as before. Some will survive, some will grow, but many will be eliminated unless these aids result in a larger total volume of business to be shared among the businesses in the field.

The foregoing raises a critical point and all attempts to help small business should be judged in terms of it. Certainly some obstacles can be removed and possibly some positive steps can be taken. But, evidently, the greatest aid to small business must be attained by bringing about those conditions (See: Bulletin No. 6 in this series) which will stimulate business in general and not just little business.

XI Policies of Big Business

Because of the importance of small business big business should give full support to the effective enforcement

of our antitrust laws, should disavow unfair and socially undesirable competitive practices. Unfair competitive practices are difficult to define, but one example might be cited—cutting prices below cost by the large concern in a given area merely to eliminate a small competitor with a view to restoring prices as soon as the small concern is liquidated.

Big business has been accused of creating a type of collectivism of its own—acquiring patents, taking on new lines, taking over a whole field, integrating operations from raw materials to consumer. These great aggregates of capital and know-how have been the source of American strength in both peace and war; few persons would break up these large units. In their expansion programs, however, the large concerns should make every effort to avoid taking unfair advantage of the smaller units and should in so far as practical take positive steps * to see that many smaller concerns are kept alive and prosperous. This will not only add to the strength of the nation but will also reduce the opportunities of the demagogue to bait the larger concerns.

XII Special Aid to Small Business

While many modern tendencies favor large business, an enormous amount of effort has been made in the last two decades to discover the handicaps of small business

* In a middle western city a number of large concerns entered an agreement to do technical research for a number of small businesses on a cost basis.
and find remedies for its difficulties. The Department of Commerce of the national government has created a Small Business Unit in charge of a staff of people in full sympathy with the problems of small business. In November, 1943, this unit published a summary of 390 (note the large number!) bills introduced in Congress from 1933 to 1943 to help small business.

Twenty-six of these bills were passed by Congress. Some are designed to help raise capital for small business from both private and public sources. The U. S. House and Senate have set up special committees, under Representative Wright Patman and Senator James E. Murray, respectively, to study the problems of small business. Both committees carry on continuous study and research, hold hearings, and make recommendations to Congress in the form of remedial and corrective legislation. These committees have the dual task of aiding small business enterprises to make adjustments to wartime conditions, as well as the broader problem of determining means of preserving small business as an essential part of our peacetime economy.

One bill which was passed was designed to reduce the complexities of government reports required of all businesses, but which bore very heavily upon small business because the smaller units do not always have adequate staffs of attorneys, accountants, etc. Fifty-four bills have been introduced to sponsor business and industry research, some of which would require or stimulate cooperative research with state universities in both technical and business administration matters.

It is generally agreed that government controls, regulations and rules bear much more heavily upon small business than on larger units. The larger ones with more adequate reserves are more adaptable and flexible and find compliance easier. Much study has gone into this question and in a few cases very small concerns have been exempted from the controls or laws.

Many people, however, question the wisdom of such special exemptions on the ground that they are open to abuse (every one will strive to get the benefit of the exemption and escape the prohibition) and on the ground that all businesses should operate under the same "rules of the game" with special privileges to none. Once special privileges are provided, enormous pressures are built up to keep on expanding the coverage.

For this reason, proposals for any special privileges for small business should be carefully examined to be certain that they comply with the American conception of fair play, uniformity of treatment, equality of opportunity for all and special privilege to none.*

Whether a specific proposal constitutes special privilege or violates the American principle of uniformity of treatment is not merely a matter of what the law carrying out the proposal states but, also, how it is administered. More abuses and evils often arise from the administration of a law than can be directly traced to the intent of those who framed and passed the law.

If small business has special difficulty of raising capital and new provisions are made to provide capital, every business should have access to this capital. If our present taxes on business discourage expansion and growth, we should provide proper relief for all business, on the

* Our federal income tax laws favor, chiefly for administrative reasons, companies with very small net income. Partnerships are favored over corporations since the latter are liable to taxation on company income and their stockholders are likewise liable for personal income taxes. Chain store taxes are designed to aid small business but are open to question because they tend to penalize efficiency.
theory that the able managers—even though in small business—will then have an opportunity to expand. If the government carries on special research it should be made available to all, on the assumption that the small units will probably have a high inducement to utilize the opportunity, while the larger units, although not barred from using it, nevertheless, will be capable of carrying on their own research and, in most instances, will do so.

An enormous number of voluntary business organizations have come into existence to promote business. All these groups are open to small business and each organization is designed to promote the interests of its members. Thus, we have over 8,000 local chambers of commerce, 3,000 national and interstate trade associations, over 5,000 local trade associations, and many other groups such as the Chamber of Commerce of the United States of America, the National Association of Manufacturers, and others. In addition, there are hundreds of professional groups, such as chemists' associations, engineers' associations, etc.

Each group generally publishes a magazine keeping its members informed of new developments, new opportunities, methods of reducing costs, promoting business and removing obstacles. In addition, most groups issue special reports on specific subjects, have a consultation service, hold meetings and provide data and materials upon request. The small employer may not belong to as many groups as he might and, therefore, is not always placed in touch with the new as promptly as might be the case but every effort should be made to extend the services of these voluntary groups to the small business unit and considerable progress has been made in this direction.

In spite of the difficulties facing small business many such units are launched, thrive and grow. This has led some observers to believe that the key to the small business problem is better management; that is, businessmen who are more competent, more aggressive, more alert, better informed, so that they may become better managers. According to this diagnosis, the solution must be found in furnishing management with better tools for management. To this end, it is proposed in the Mead-Lea bill, now pending in Congress, that the federal government provide a management consulting service for business. Consultants highly qualified in finance, purchasing, production, distribution and marketing, personnel, etc., would be stationed throughout the country to provide on-the-spot advice and help in the solution of all problems. They would put the management in touch with all varieties of information and possible sources of information. This type of aid would be comparable to that now furnished, at great cost, to farmers in over 3,000 counties through the county agents and other agricultural services.

Another proposal is to have the federal government subsidize business research through the state universities on the same basis as agricultural research is now subsidized through the numerous agricultural stations and state universities throughout the country.

Both of these proposals have merit but the aid should not be restricted to businesses of any given size. Some people see some danger in such proposals on the ground that they might lead to undue interference and control of business, but, if properly safeguarded, this danger can be avoided.

Another proposal relates to the supply of capital. Small businesses, because they frequently are not firmly established and have not grown by their own strength, may have plans for new products, for promotion, etc., but
lack capital. Government capital loaned to such enterprises might entail considerable dangers. Political pressures would inevitably play a role in determining which companies should secure loans and if the government has a stake in an enterprise it would also insist in having a voice in management, which might lead to undue invasion of a field in which government should not play a role according to our traditional conception of the place of government in the economy.

A better solution may be found by having groups of banks, investment houses, and perhaps insurance companies set up special services for making loans to small business and buying stock in small companies. By pooling the risks and making a small insurance charge to cover the inevitable losses, much new venture capital could be furnished by private enterprise on a sound basis without getting our government involved in all sorts of ventures.

In the past 20 years some 15,000 local banks have disappeared. Either the banks, as such, or their officers supplied venture capital to local people with inventions, or ideas for new business. With the shrinkage in this source of capital, the financial aid for new business has been diminished. Savings have tended to be absorbed by government bonds, which type of investment normally does not lead to the creation of continuously self-sustaining job opportunities. With proper encouragement, through a revision of our system of business taxation, there is reason to believe that in hundreds of communities local businessmen, people with funds or having access to funds, would be willing to subscribe to new stock issues for new or expanded concerns. Every substantial community might have a Venture Capital Inc., which would specialize in sifting proposals for new businesses or requests for new capital and would purchase shares in the proposed ventures if found such as to warrant some hope of success. This local sifting, appraisal and financing is highly desirable.

Only a small number of business concerns have profits year after year. Even in prosperous years, about one-third of our corporations have no profits. The owners have to pocket the losses in the bad years and when profits do occur governments (both state and federal) take from 20% to 80% of the profits.

Under this situation, the new or small concern finds considerable difficulty in getting started or building up adequate working capital or capital for expansion. Thus, it has been proposed that all new businesses be exempt from the income tax law for several years, or that they be allowed to carry forward their losses so they would pay income tax on the average earnings for a period of say 5 years, rather than to have the government skim the cream in the few good years and force the owners to absorb the losses of the bad years.

Again, these proposals have merit, although they would raise some administrative problems and might be open to abuse.

XIII Conclusions

1. Small businesses have special problems because of their size.
2. For both political and economic reasons, the establishment and survival of many small businesses are important.
3. It is impossible to prescribe any simple remedy for the problems of small business.
4. The almost universal desire for a healthy, expanding, small business in this country should assure us that some of the obstacles to small business will be removed.

5. If general economic conditions are favorable, small business will be able to keep its place and to grow in size and importance.

6. The chief difficulties of small business have been due to conditions which hindered all business, not just small business.

7. Special remedies or special privileges for small business may be of doubtful value, and in any case should be adopted only after the most thoughtful consideration as to their efficacy.

8. Should government or private groups provide special aid to small business, abuses are less likely to develop if such aid is made available to firms of all sizes.

A thorough discussion and understanding of the problems of small business are essential steps for developing a program of action. The problem is not simple—which explains why the 390 bills in behalf of small business introduced in Congress have not established any general agreement on what should be done.

The mere awareness of the fact of the problem and its nature should gradually encourage those steps which will ease the problem.

* What is meant may be seen in Bulletin No. 6, The Problem of Business Incentives.

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2204