

# The Nature & Importance of Small Business

## What is 'Small Business'?

- Small businesses are differentiated from other businesses by qualitative & quantitative criteria.
  - Quantitative criteria: asset value, number of employees, value and volume of turnover, capital requirements, the amount of profit earned, and market share.
  - Qualitative criteria: management decision-making process, ownership interest and markets served.
- In Australia, a small business is identified by the following characteristics:
  - independent ownership
  - close control by the owners who are responsible for the principal decisions of the enterprise
  - owner supplied capital and operation
  - localised operations (although markets may be overseas)
  - relatively small market share
- The *Corporations Act 2001* defines a small proprietary company as one with the following characteristics (if two are unsatisfied, it is a large propriety company):
  - consolidated revenue < \$25 million
  - consolidated gross assets < \$12.5 million
  - < 50 employees
- The most widely used definition of small business is that proposed by Australian Bureau of Statistics (ABS) which is what we use in this unit.
  - The ABS define 'small business' as a business employing fewer than 20 employees.
  - However, there are various classes of small businesses within this broad definition. A small business may be non-employing, a micro-business (1-4 employees), or small (5-19 workers).

## Economic Relevance of Small Business

- The small business sector *comprises a major percentage of all private sector businesses*.
  - Of the total 2,313,291 actively trading businesses in Australia at the end of June 2018, about 97.7% or 2,259,098 were small-sized (Australian Small Business and Family Enterprise Ombudsman, 2019). These all contribute to GDP.
- The small business sector is *a major source of employment*.
  - The sector was responsible for 44% of total private sector industry employment for the financial year to June 2018 (Australian Small Business and Family Enterprise Ombudsman, 2019).
- Small businesses *disperse economic activity throughout the country*, thus reducing rural-urban migration and concentration of economic activity in urban areas.
  - In this regard they are important to regional development. Approximately 35.2% of small businesses operate in regional and remote Australia (DIISR&TE, 2011, p. 23).
- In the 2017-2018 financial year, the small business sector contributed about 34% to *industry value added*, specifically 75% of the agriculture, forestry and fishing industry.
- Small businesses *provide revenue for the government* through taxation of their income and the income of those they employ.
- They *mobilise domestic savings for investment* through their cash savings and deposits.

- Small businesses add value by *processing raw materials before export*. For the 2016 - 2017 financial year, 59% of small businesses exported goods (Australian Small Business and Family Enterprise Ombudsman, 2019).
  - By *producing for export and import substitution*, small businesses help to improve the balance of payment situation in a country.
- Small businesses provide *training grounds for first time employees* through apprenticeships, traineeships and internships. Many school leavers start their first jobs in small businesses.
  - Small business provide 67% of workers with their first jobs and basic job training.
- Small businesses constitute an important *source of innovation*.
  - They introduce new or significantly improved products or services, operational process, organisational / managerial process or marketing methods.
  - However, in the 2016-2017 financial year, 50% of firms employing 5-19 people introduced a new innovation compared with 62.8% for large firms (Australian Small Business and Family Enterprise Ombudsman, 2019).
- Cultural diversity of entrepreneurship:
  - *Young people*: Generation Y (1980-2000) is one of the most entrepreneurial generations in history.
  - *Women*: 35% of small business owners in Australia are women.
  - *Immigrants*: a third of small business owners are migrants and they employ 1.41 million Australians (CGU Migrant Business Report, 2018).

## Why the Interest in Small Business?

- *Recognition and accomplishment*: globally, successful entrepreneurs have hero status, such as Michael Dell (Dell Computers), Richard Branson (Virgin) and Mark Zuckerberg (Facebook), and serve as role models for aspiring entrepreneurs.
- *Shift to a service/knowledge economy*: the move to a knowledge-based economy and the focus on service is another factor fuelling the growth of small businesses in Australia.
  - The service sector accounts for 83.9% of all small business (DIISR&TE, 2012, p.30).
  - Because of their relatively low start-up costs, service businesses have been very popular with entrepreneurs.
- *Technology advancements*: technology has made it easier to start and operate a business at a low cost. Ready access to phones, computers, printers, scanners and other such devices means anyone can start a small business and achieve a competitive edge over other businesses.
  - One recent survey by AT&T reports that 96% of small businesses use wireless technology and 64% of owners say that their companies could not survive without it.
- *Outsourcing*: entrepreneurs can outsource many of the operations of their companies and retain only those in which they have a competitive advantage.
- *Employment avenue for retrenched employees* of large firms that are downsizing.
- *International opportunities*: small businesses can find business opportunities worldwide, which is made easy via the Internet.
- *Innovation*: independent inventors and small businesses account for a significant number of new products and services.
- *Ability to respond to change*: the organic structures of small firms provide greater speed of action than the mechanistic structures of large firms, enabling them to more readily adapt to changing market conditions
- *New attitudes to work*: Employees are demanding higher quality work environments where they can express their creative skills and use their own initiatives, which small business provide.

- *Big businesses need small businesses*: Many big businesses rely on small businesses to either produce component parts or distribute their products. Also the idea that “*small is beautiful*”

## Advantages of Owning a Small Business

- *Independence*: the opportunity to be one's own boss, to work for oneself and to have the freedom to adopt one's own work approach. It also covers the ability to control one's own time, to choose the people to work with and the opportunity to lead rather than be led by others
- *Escape*: independent business operation can provide an escape from unpleasant work environments and from the frustration of working with an unreasonable boss.
- *Recognition and accomplishment*: developing a new product idea and contributing to the success of a business provides the owner with a personal sense of accomplishment
  - Owners gain social recognition for their achievements, raising the status and prestige of their families. They gain respect among friends and members of the community
- *Wealth creation*: successful business operation brings financial rewards, raising the economic status of the owner and his or her family.
- *Unlimited career paths*: opens new windows of opportunity to the owner as it provides increased access to information, people and resources.
- *Accommodation*: greater flexibility in personal life; it enables the owner to work at home or at other desirable locations, and to spend more time with family members (who may also then get to be part of the business).
- *Contribution to community/society*: they are given positions of respect in the community and can influence the development of their communities. Successful business operation therefore provides an opportunity to contribute to community development.

## Disadvantages of Small Business Ownership

- *Risk of failure*: particularly high for small and new firms due to limited access to resources and markets, referred to as the liability of newness and smallness.
  - Small firms with new products are particularly vulnerable, as it is difficult to effectively assess the market or demand for these products before they are launched.
  - This leads to the *risk of losing your entire invested capital*.
- *Long hours of work*: for relatively little financial reward, particularly during the early stages of the business. Owners are rarely able to take time off for vacation or leisure.
  - The average small business owner works 54 hours per week, compared to the typical 35.
- *High levels of stress*: from loneliness, immersion in business, people problems, lack of skills in interpersonal and human relations, failure to delegate and a strong desire to achieve
- *Disjointed family life and low quality of life*: marriages and friendships are often casualties of small business ownership.
  - The family savings may be used for capital and, in the early stages where returns are very low or non-existent, the family's standard of living diminished.
  - Families of business owners often live on the income of one parent. In several cases, spouses and children provide support by working long hours in the business for little or no reward.
- *Uncertainty of income*: in the early years of operation there is considerable uncertainty about income to be generated from the business
- *Complete responsibilities*: many entrepreneurs find that they must make decisions on issues about which they are not really knowledgeable.