

The State of the Small Business Economy in the Pandemic

U.S. House of Representatives Committee on Small Business

February 4, 2021

Testimony by:

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Thank you, Chair Velázquez, Ranking member Luetkemeyer, and members of the Committee. It is an honor to testify before you on the state of the small business economy. I am a Professor of Economics at the University of California, Santa Cruz and have studied entrepreneurship, racial inequality and small business policy for over 25 years. I have been asked to discuss the findings from my research on the impacts of the pandemic on small business owners.

Small businesses across the country are struggling. Minority-owned businesses are especially struggling.

As you know, obtaining up-to-date and accurate information on the effects of the pandemic on small business owners has been extremely difficult. I have spent the past eight months compiling and analyzing data on how small businesses are faring during the pandemic.

I have focused my research on three main questions. First, what happened to small business owners? Did the pandemic disproportionately close minority-owned businesses? Second, how much did small businesses lose in sales during the early stages of the pandemic? What types of businesses were hit the hardest? Third, did the massive, unprecedented levels of government relief for small businesses through the PPP and EIDL programs get distributed evenly to minority communities?

Small Business Activity in the Pandemic

On March 19, 2020, the State of California imposed shelter-in-place restrictions with New York State following the next day. By early April most states imposed social distancing restrictions that closed “non-essential” businesses and added to consumer health concerns in the emerging pandemic.

In my research, I found that the number of active business owners in the U.S. plummeted by 3.3 million or 22 percent over the crucial two-month window from February to April 2020 (Figure 1).¹ No other one-, two- or even 12-month window of time has ever shown such a large change in business activity. For comparison, from the start to the end of the Great Recession the number of active business owners dropped by only 5 percent.

African-American businesses were hit the hardest experiencing a 41 percent drop in business activity (Figure 2). Latinx business owner activity fell by 32 percent, and Asian business owner activity dropped by 26 percent. Unfavorable industry concentrations and the smaller scale of businesses owned by minorities were partly responsible.

Extending the analysis into May and June small business activity partially rebounded in both months. But, the disproportionate impacts from COVID-19 by race lingered. African-Americans continued to experience the largest losses, with 26 percent of business owners still not active in May and 19 percent not active in June. Job losses were also

¹ Fairlie, Robert W. 2020. "The impact of COVID-19 on small business owners: The first three months after social-distancing restrictions." *Journal of Economics & Management Strategy*, 29(4): 727-740.

much higher for minority workers.² Black unemployment hit a peak of 17 percent and Latinx unemployment hit a peak of 18 percent.

Although many of the closures in April, May and June turned out to be temporary, any month of closure is problematic because it reflects lost income to the owner of the business. The owner still has to pay rent, some employees and other expenses.

Sales Losses in the Pandemic

It has been especially difficult to figure out how much small businesses have lost in sales and revenues in the pandemic. We suspect that losses have been great but data on actual losses in sales are difficult to find.

Using taxable sales data from the California Department of Tax and Fee Administration, we found average sales losses of 17 percent in the second quarter of 2020. Normal year-over-year growth is in the range of 3-4 percent.³ Sales losses were largest in businesses affected by mandatory lockdowns. For example, hotels lost 91 percent, restaurants lost 61 percent, and clothing stores lost 56 percent (Table 1).

The losses among so many different types of businesses are disconcerting, but perhaps even more troubling are consumer trends away from in-person stores to shopping online. At the same time in-store purchases were sharply declining online sales grew by 180 percent in the second quarter of 2020.

The large losses in sales in the second quarter of 2020 are worrisome for the longer-term survival of small, local businesses throughout the country. Although larger stores and chains with a strong online presence may survive, many small businesses will not have the resources to weather a prolonged recovery. Recent Census Bureau surveys indicate that only 15-20 percent of small businesses have enough cash on hand to cover 3 months of operations.⁴

Financial Help to Small Businesses in the Pandemic

One of the stated goals in the CARES Act was to prioritize serving “underserved markets” and businesses owned by “socially and economically disadvantaged individuals.” Did the PPP and EIDL programs, which were key components of the CARES Act, get distributed to minority communities providing much needed help to the businesses, employees and residents of those communities?

² Couch, Kenneth A., Robert Fairlie, and Huanan Xu. 2020. "Early evidence of the impacts of COVID-19 on minority unemployment." *Journal of Public Economics* 192.

³ Fairlie, Robert, and Frank Fossen. 2021. "Sales Losses in the First Quarter of the COVID-19 Pandemic: Evidence from California Administrative Data," NBER Working Paper No. 28414.

⁴ U.S. Census Bureau. 2020. "Small Business Pulse Survey," <https://portal.census.gov/pulse/data/>.

Using data on 15 million individual loans, we found that funding from these relief programs both flowed to minority communities and away from minority communities.⁵ If anything we found a slightly positive relationship between PPP loan receipt per business and the minority share of the population. There is some evidence, however, that the first round of funds was disproportionately distributed to non-minority communities and the second round of funds was disproportionately distributed to minority communities. When focusing on PPP loan amounts per employee, however, we find a negative relationship with minority communities. In contrast, EIDL loans and advances, in both number and amounts, were provided to minority communities.

Recent Reversal of Progress for Business Owners

In my continual work tracking how small businesses are doing in the recovery I recently found some alarming trends. From April to October there was constant month-to-month improvement in business activity, but in November and December that pattern reversed. From October to December small business activity dropped by 6 percent (Figure 3).⁶ For minority owners the drop was from 5-10 percent (Table 2).

Vulnerable Groups

The losses that I have described here are especially alarming for two vulnerable groups, African-Americans and Latinx. Prior to the pandemic, business ownership as a share of the population and average revenues per business were already low for both groups.⁷ But, perhaps more importantly there is a huge wealth gap. Half of black families in the U.S. have less than \$10,000 in total wealth and half of Latinx families have less than \$25,000 in total wealth. White levels of wealth are 7 to 18 times higher. Many minority business owners will simply not have the financial resources to weather prolonged closures.

Four things that could help.

I would like to turn to discussing what could help us move forward.

1. First, consumers need to feel safe again. The number one priority for helping small businesses is to get the vaccine out faster. People are anxious to get back to restaurants, bars and shops. Pent-up demand should help kick start the small business recovery.
2. Second, more financial assistance is needed for small business owners especially during the next few months. In particular, rent relief and protection could be crucial for survival.

⁵ Fairlie, Robert, and Frank Fossen. 2021. "Did the \$660 Billion Paycheck Protection Program and \$220 Billion Economic Injury Disaster Loan Program Get Disbursed to Minority Communities in the Early Stages of COVID-19?" NBER Working Paper No. 28321.

⁶ See <https://people.ucsc.edu/~rfairlie/current/>.

⁷ Fairlie, Robert. "Racial Inequality in Business Ownership and Income" *Oxford Review of Economic Policy*, 34(4): 597–614, 2018. Fairlie, Robert and Alicia Robb. *Race and Entrepreneurial Success: Black-, Asian-, and White-Owned Businesses in the United States*, Cambridge: MIT Press, 2008.

3. Third, we need to slow down the extensive shift to online shopping which was happening prior to the pandemic. This trend is unlikely to stop. Small businesses need to have more of an online presence. Aid in the form of web page assistance could be useful. Search engines could prioritize local small businesses instead of online retailers and big box stores.

4. Fourth, the federal government needs to collect more data on race in their relief efforts. Demographic information was only partially and unevenly collected in the first two rounds providing PPP funds, and there was much criticism for this omission. The information is crucial for future research on equity issues. Additionally, collection of information on applications for loans that were denied would be useful.

In closing, we need to reverse the negative impacts of the pandemic on minority-owned businesses. These losses are problematic for broader racial inequality because of the importance of small businesses for local job creation, economic advancement, and longer-term wealth gaps. Losses from the pandemic are also very costly to total U.S. productivity as minority-owned businesses represent the fastest growing segment of the business population. Finally, we will lose the vibrant downtowns with diverse restaurants and shops that truly make America great.

Thank you for the opportunity to present the findings from my research on this topic. I look forward to hearing your comments and questions.

Figure 1
Number of Active Business Owners in the United States (January 2000 - April 2020)

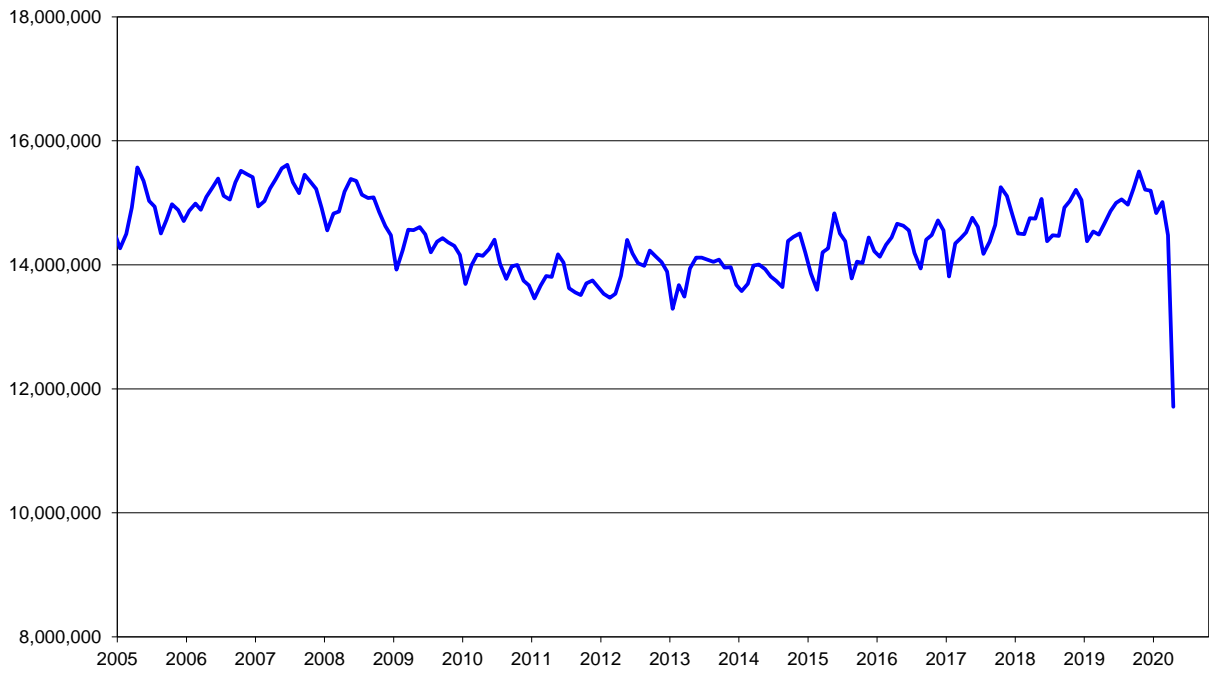


Figure 2: Losses in the Number of Active Business Owners before and after COVID-19 Restrictions (February to April 2020)

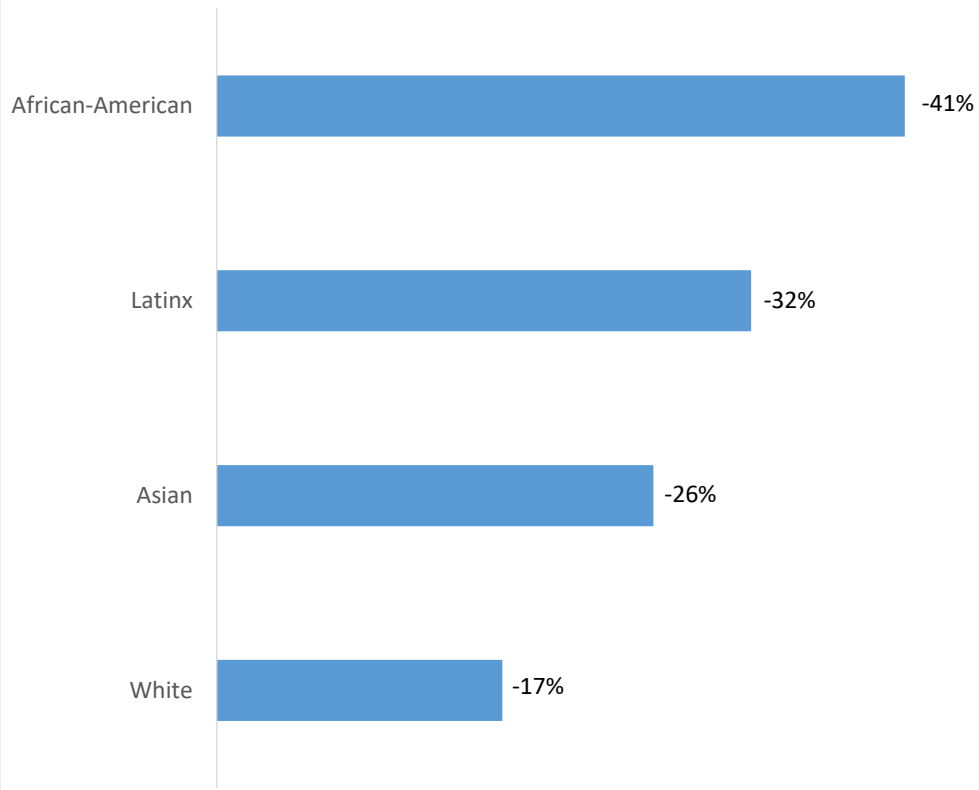


Figure 3
Number of Active Business Owners in the United States (Jan. 2019 - Dec. 2020)

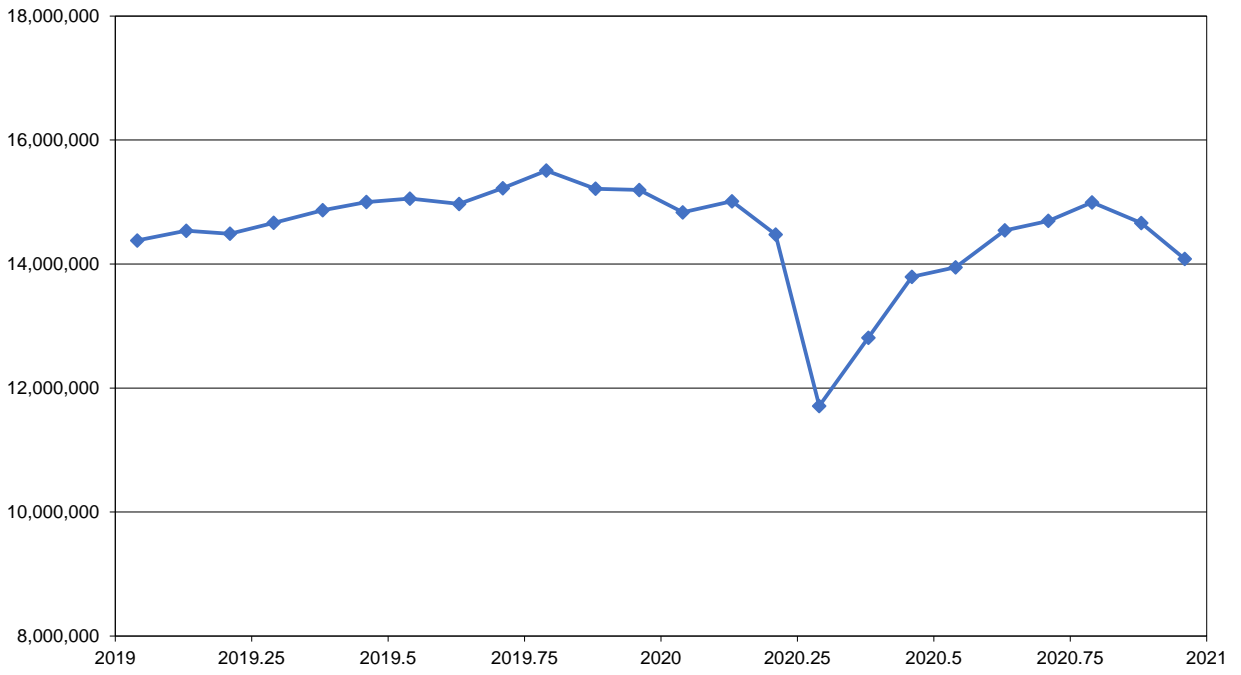


Table 1: California Taxable Sales Losses by Subsector Business Types

Business Type	Percent Change 2019Q2 to 2020Q2	Taxable Transactions Amount	Business Type	Percent Change 2019Q2 to 2020Q2	Taxable Transactions Amount
Total All Outlets	-17	152,362,296,481	Miscellaneous Store Retailers	-17	4,418,659,674
Total Retail and Food Services	-17	105,528,311,167	Florists	-39	103,717,354
Motor Vehicle and Parts Dealers	-15	19,294,245,937	Office Supplies and Stationery Stores	-22	642,964,260
New Car Dealers	-16	13,661,226,032	Gift, Novelty, and Souvenir Stores	-58	197,790,991
Used Car Dealers	-27	2,017,580,937	Used Merchandise Stores	-44	144,130,178
Other Motor Vehicle Dealers	11	1,546,237,177	Other Miscellaneous Store Retailers	-8	3,330,056,891
Automotive Parts, Access. and Tires	-3	2,069,201,791	Nonstore Retailers	181	13,273,550,077
Furniture and Home Furn. Stores	-18	2,625,229,637	Food Services and Drinking Places	-47	11,991,170,465
Furniture Stores	-28	1,532,455,251	Special Food Services	-76	292,967,418
Home Furnishings Stores	3	1,092,774,386	Drinking Places (Alcoholic Beverages)	-86	65,185,094
Electronics and Appliance Stores	-14	3,663,719,124	Full-Service Restaurants	-61	4,454,731,382
Building Material and Garden Equipment	12	12,248,068,380	Limited-Service Eating Places	-25	7,178,286,571
Building Material and Supplies Dealers	13	11,064,090,950	Total All Other Outlets	-19	46,833,985,314
Lawn and Garden Equipment and Supplies	7	1,183,977,430	Agriculture, Forestry, Fishing and Hunting	40	325,549,091
Food and Beverage Stores	2	7,584,295,812	Mining, Quarrying, and Oil and Gas Extraction	-29	139,003,233
Supermarkets and Other Grocery Stores	5	5,209,119,995	Utilities	0	364,305,709
Convenience Stores	-12	841,092,239	Construction	-17	2,305,307,376
Specialty Food Stores	-40	202,729,466	Manufacturing	-13	11,005,456,107
Beer, Wine, and Liquor Stores	10	1,331,354,112	Wholesale Trade	-17	18,392,665,466
Health and Personal Care Stores	-11	3,414,123,225	Transportation and Warehousing	-40	408,491,412
Pharmacies and Drug Stores	7	2,024,226,564	Information	-9	1,960,180,852
Other Health and Personal Care Stores	-28	1,389,896,661	Finance and Insurance	-6	340,123,180
Gasoline Stations	-47	7,737,896,946	Real Estate and Rental and Leasing	-19	5,872,138,743
Clothing and Clothing Access. Stores	-54	4,744,372,982	Professional, Scientific, and Technical Service	0	1,893,493,925
Clothing Stores	-56	3,640,766,921	Management of Companies and Enterprises	-18	6,432,654
Shoe Stores	-38	648,398,066	Administrative and Support and Waste Management and Remediation Services	-39	597,633,328
Jewelry, Luggage, and Leather Goods Stores	-61	455,207,995	Educational Services	-47	163,539,655
Sporting Goods, Hobby, Mus. Inst., Book Stores	-20	2,010,965,666	Health Care and Social Assistance	-15	286,043,742
Sporting Goods Stores	0	1,257,390,598	Arts, Entertainment, and Recreation	-83	188,119,522
Hobby, Toy and Musical Instrument Stores	-30	553,514,156	Accommodation	-92	94,715,762
Book Stores and News Dealers	-55	200,060,912	Other Services (except Public Administration)	-31	2,145,100,206
General Merchandise Stores	-10	12,522,013,242	Public Administration	-11	103,363,587
			Others	59	242,321,764

Table 2: Change in Number of Active Business Owners in the United States (Minority Groups)

	African-American				Latinx				Asian			
	Number	Relative to: Month in Reg.			Number	Relative to: Month in Reg.			Number	Relative to: Month in Reg.		
	Feb. 2020	Prev. Yr.	Adjusted	Feb. 2020	Prev. Yr.	Adjusted	Feb. 2020	Prev. Yr.	Adjusted	Feb. 2020	Prev. Yr.	Adjusted
Feb. 2020	1,079,116	0%	2%	0%	2,070,896	0%	5%	0%	888,528	0%	-1%	0%
Mar. 2020	1,074,478	0%	13%	-6%	1,936,739	-6%	-3%	-4%	936,072	5%	4%	6%
Apr. 2020	637,769	-41%	-38%	-52%	1,412,925	-32%	-28%	-32%	657,896	-26%	-36%	-29%
May 2020	798,668	-26%	-23%	-35%	1,668,254	-19%	-14%	-20%	700,393	-21%	-24%	-24%
June 2020	872,717	-19%	-24%	-28%	1,855,026	-10%	-4%	-8%	798,811	-10%	-14%	-10%
July 2020	974,093	-10%	-18%	-18%	1,851,702	-11%	0%	-10%	809,922	-9%	-5%	-7%
Aug. 2020	1,084,869	1%	-2%	-5%	2,009,642	-3%	2%	-3%	794,433	-11%	-11%	-9%
Sept. 2020	1,103,761	2%	-6%	-6%	2,093,925	1%	0%	0%	741,249	-17%	-12%	-20%
Oct. 2020	1,153,326	7%	-3%	-4%	2,130,408	3%	1%	-1%	758,205	-15%	-5%	-17%
Nov. 2020	1,115,874	3%	0%	-5%	2,169,500	5%	-1%	-2%	692,402	-22%	-16%	-27%
Dec. 2020	1,046,956	-3%	-10%	-12%	2,004,637	-3%	-1%	-7%	713,485	-20%	-20%	-23%

Notes: (1) Estimates are continuation from those reported in Fairlie, Robert. 2020. "The Impact of COVID-19 on Small Business Owners: The First Three Months after Social-Distancing Restrictions" *Journal of Economics and Management Strategy*. (2) Reg. Adjusted estimates are based on regression analysis accounting for trends and seasonality (monthly).