

The Future of Small Business: Supporting Entrepreneurs in the Post-Crisis Era

Digital Entrepreneurship White Paper

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America's 32 million small businesses are focused on surviving the COVID-19 crisis. Those that survive will emerge into a different world.

The purpose of this paper is to generate ideas about how to best support small businesses and entrepreneurs post-crisis, over the next 1-5 years.

Even before the COVID-19 crisis, small businesses and entrepreneurs were under pressure. Across most industries, markets have become more concentrated. A few large firms have been capturing greater market share, and a greater share of the profits, in the US (Covarrubias, Gutiérrez, & Philippon, 2020). New business formation has been decreasing in the US over the past four decades (Goldschlag & Tabarrok, 2018). At the 'low-end' of entrepreneurship, however, gig economy contracting continues to grow. Over 57 million Americans reported some freelancing income in 2018 (Ozimek, 2019).

How can we help small businesses survive in the longer term? A good place to start is with the competitive advantages that small businesses have, and how those advantages might be changing.

We begin with the fundamental question: why do small businesses exist? What is their role in a modern economy? And will the transition to a post-crisis environment help or hurt small businesses?

Why do small businesses exist?

With the vast majority of US businesses being small, it might seem strange to ask why they exist. When do small businesses have an advantage over their larger competitors?

Unique advantages of small businesses

An early study (Stoner, 1987) listed the most common unique advantage reported by small businesses themselves, in order of frequency:

- Unique skills, knowledge, or experience of employees
- Unique product or service
- Better customer service
- Location
- Low cost

The most frequently reported sources of competitive advantage for small businesses are based on what they know, what they provide, and how they provide it. The good news is that in a complex, rapidly-changing economy, many new situations and customer needs will emerge in which unique knowledge and skills will be valuable. To the extent that entrepreneurs are able to translate their knowledge into unique services and/or better customer insight that are viable on a smaller scale, small businesses have the advantage.

Widespread selling on digital platforms, however, will put pressure on those small businesses who simply distribute or support products made by others. Larger businesses can also use new automation and personalization technology to erode the customer service advantage of small businesses.

For small businesses based on unique location, new digital modes of distribution will be a survival threat. Some of these businesses will have to transform into more of a community institution, or local charity, in order to survive. For small businesses to compete on cost, their advantage will depend more on lower labor costs than lower material, product, or capital costs. With online platforms allowing large businesses to source low-cost labor easily, this advantage will also be under threat.

Strategic advantages (and disadvantages) of small business

More recent theories of competitive advantage focus on the combination of a business' unique assets, and its unique processes or activities. Control over valuable resources is the 'resource-based view' of strategic advantage, while the ability to learn and act in new ways are a company's 'dynamic capabilities' (Ko & Liu, 2017).

Examples of Competitive Assets	Examples of Competitive Activities
People	Marketing
Finance	Research & Development
Technology	Customization
Infrastructure	Quality

With the exception of unique people, particularly the founder or founders, small businesses don't normally have the advantage in terms of asset access or control. Large businesses have access to almost free money in an era of zero interest rates, can deploy complex new technologies, and have the size to bargain with infrastructure providers. Small businesses instead need to rely on competitive activity, by keeping close contact with customers, developing a new technology or technique, or creating a specialized new product or service.

Small business flexibility

A final important advantage of small businesses is their flexibility (Hatten, 2018). Small businesses provide output flexibility, particularly in volatile industries, as contractors or franchisees for larger businesses (Fiegenbaum & Karnani, 1991). The role of small businesses in this view is to act as a set of resources that larger businesses can use to manage their costs and risks, without having to take on new employees or make new investments themselves.

While this contractor or freelancer world offers the possibility of freedom for a small business, the risk is that digital platforms will become the dominant means of securing work, and capture an ever-increasing share of the value created by contractors and freelancers. In an extreme version of this scenario, small businesses and entrepreneurs will exist to serve the needs of large business, and to disappear gracefully when their needs change.

How to help small businesses in the longer term

Based on their unique advantages, and the new threats they face, we offer preliminary thoughts on how to support small business in the longer term. The summary list is below.

- 1. Make direct help more effective**
- 2. One size doesn't fit all - target assistance to source of competitive advantage**
- 3. Platforms that act like co-ops**
- 4. Local businesses as community resources**
- 5. Provide pivot support**
- 6. Provide sector expertise**
- 7. Provide better digital starter resources**

Make direct help more effective

Sending relief payments to 32 million small businesses, plus tens of millions more freelancers and entrepreneurs, would be a challenge in the best of times. While the model of sending \$1,200 relief payments to individuals in the US through the IRS

wasn't perfect, it has been much more effective than the implementation of small business assistance.

Future assistance needs to be distributed through a government agency with experience working at scale, and with many pre-existing client relationships – more like the IRS than the Small Business Administration. Direct assistance avoids working through a private intermediary like the big banks, with their own cumbersome application procedures, client priorities, and substantial fees.

Assistance needs to be prioritized and targeted, as seen by the outcry when larger firms and even publicly traded companies received small business bailout funds first. Targeting should prioritize the smallest and most in need, rather than the larger businesses who were best able to navigate a complex application process. Eligibility criteria should be based on objective data that already exists, such as past revenue reported in tax filings, rather than asking businesses to prove a 30% or 50% revenue loss during the middle of a crisis.

One size doesn't fit all – target assistance to source of competitive advantage

Small business and entrepreneurship isn't one size fits all. We can see from the discussion of competitive advantage that there are at least two worlds of small business. One world of small businesses competes primarily on innovation, customer contact, and unique knowledge and skills. And we have a huge and growing world of small businesses and freelancers that compete on flexibility and low total labor cost.

For the first group, their task is to increase innovation, and intensify the search for new customer needs and new solutions. They need investment help, coaching, and innovation assistance.

For the second group, their economic fate during a massive shutdown is to provide flexibility by shutting themselves down. This group is now too large and too economically significant to simply allow them to fail as businesses. They need well-targeted subsidies and assistance to ride out the storm, along with legal and mediation services. They also need socially-supported mechanisms to develop resource cushions for the inevitable ups and downs of the economy. Future recessions will not treat the freelancer economy kindly.

Platforms that act like co-ops

More small businesses, entrepreneurs, and freelancers are doing business through digital platforms. So far, the business models of early platforms like Uber, Airbnb, and app stores have captured transaction fees from 10-30%, and established dominant control over the operations of their marketplaces. Restaurants who tried to pivot to

home delivery faced these high transaction costs on dominant delivery networks like DoorDash, which at their profit margin level was an unsustainable cost.

If these work and business platforms will be a significant part of small business revenue in the future, at least some of these digital platforms need to be designed and governed as neutral infrastructure, and run in the interests of their members. Once a digital platform controls a market through its customer access, its detailed data, and its opaque algorithms, the temptation to maximize its own revenue will be too great. The societal advantages of a flourishing world of small businesses and entrepreneurs will vastly outweigh the lost revenue of the new monopolists. The technology infrastructure for these platforms can be provided incredibly cheaply at scale, as shown by examples such as craigslist.

Local businesses as community resources

A fraction of traditional local businesses will not be economically viable in the same way after the crisis. These beloved restaurants, bars, and bookshops will need to be treated more like community resources, or a kind of hybrid social enterprise.

We see this in the many fundraising appeals online for local businesses. If a local business is able to establish itself as a community resource or institution, the appetite to support them through donations and other nonprofit revenue is there. For example, the iconic City Lights Bookstore in San Francisco raised almost half a million dollars in just a few days.

More local businesses will need to establish their viability through fundraising and other non-customer revenue. There's not a playbook for this new model yet, beyond starting a GoFundMe page. Local businesses will need good advice on how to navigate becoming a social enterprise, based on nonprofit and social enterprise research. The goodwill that American consumers express for small businesses often doesn't translate to purchases if there's any cost difference, so other strategies will be needed.

Provide pivot support

Some small businesses had no choice but to try making a completely different product or service, for example an alcohol distillery switching to hand sanitizer production. Cities such as Vancouver, Canada created innovative loan funds specifically targeted to helping small businesses make a product change. Other kinds of pivots, such as restaurants switching to catered meals for sheltering seniors, were facilitated by local organizations who could connect restaurants with nonprofit delivery services, and clients in need.

Small businesses would benefit from a deliberate campaign to help them prepare them for pivoting during future economic shocks, including public crises. Every small

business should be creating their Plan B, and maybe even trying it, before the next crisis or downturn. This kind of innovation search based on core competencies should probably be a permanent part of every small business' future.

Provide sector expertise

Small businesses and entrepreneurs have places to turn for personalized assistance, from the SBA to small business centers run by local universities. This assistance is usually organized around functional expertise, like business planning, marketing, and finance. This leaves a gap of resources focused on helping small businesses in particular sectors. Restaurants looking for tips on how to survive, for example, have to search across many scattered resources to find ideas and success stories.

Types of Small Business, US, Ranked by Employment
Health care/Social assistance
Accommodation/Food
Retail
Manufacturing
Professional, scientific, tech services
Construction
Other Services

There need to be more support services focused on the particular needs of each of these sectors, such as the discussion group set up by a hospital to let smaller health care providers exchange ideas. The immediate tips, resources, and help needed by small manufacturers are quite different from restaurants, nail salons, or small construction companies. If nothing else, there should be decent platforms for conversation, and sharing practical tips.

Better digital starter resources

Whatever else happens in the post-crisis economy, the role of digital will increase. Both the 'high-end' of innovative, specialized entrepreneurship and the 'low-end' of flexible labor will need to function more effectively in an online business environment.

Too many of the support resources for digital businesses teach technical skills, rather than digital business and entrepreneurial skills. It's nice that entrepreneurs can learn how to build a website, or even code. It is true that a large fraction of small businesses, and perhaps even a majority, lack even a basic website. But local businesses have much more immediate needs. They need to learn how to retain existing customers, how to attract new customers, how to provide a great user experience, and how to test and measure the effectiveness of their new ideas.

Of course, we here at learndigitalentrepreneurship.com are trying to provide better digital business resources, but we were hoping and expecting to have much more competition by now. There are so many more resources available online to learn technical skills, than how to do business online. If just a fraction of that learning resource shifted to help people learn digital business, it would help small businesses and entrepreneurs survive the challenges to come.

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