TESTIMONY BEFORE THE UNITED STATES CONGRESS
ON BEHALF OF THE

NATIONAL FEDERATION OF INDEPENDENT BUSINESS

NFIB
The Voice of Small Business®

Testimony of William C. Dunkelberg

Senate Committee on Finance

March 13, 2014

Exploring Innovative Ideas and Policies That Can Strengthen the Economic Foundations of American Households and Contribute to the Growth of the Middle Class

Good morning, Chairman Wyden, Ranking Member Hatch, and members of the Committee. I am pleased to be here as the Chief Economist of the National Federation of Independent Business (NFIB), the nation's leading small business advocacy organization representing over 350,000 small businesses owners across the country.

My invitation to appear before the Committee today said that you were looking for new, innovative ways to help the small business economy, which accounts for about half of private GDP production historically, half of private employment and most of the new jobs created.[1] My suggestion is that we get back to basics first, fixing what we know is wrong before we try to overlay new "innovative" policies on the economy. The basics will provide the largest payoff to policy efforts.

The employment problem we face today is of two types: (1) cyclical, rehiring positions lost in the recession and (2) new firm creation, the source of net job growth. In simple terms, if our population grows by 3 million people, the demand for goods and services will increase and new firms will be formed. However, all demand is not alike in job creation. For instance, cars are produced with less new labor required than in services, which account for 70 percent of consumer spending. New firm creation has not attained pre-recession levels when tens of thousands of employer firms disappeared, especially in construction. In addition, existing firms have increased employment only modestly after dramatic reductions in the recession.

However, not all businesses are experiencing a slow recovery as the US economy is currently bifurcated. Manufacturing and exporting firms are growing nicely as profits hit a record share of GDP and financial markets hit record highs. The unemployment rate remains high and workers are abandoning the labor force at a far greater pace in unexpected age groups than demographic analysis would lead us to expect. Although GDP is far greater than its peak in 2007, employment remains over one million below its peak (January, 2008). Measures of economic activity monitored by the National Federation of Independent Business[2] over the past 40 years make it clear that the small business sector has not successfully emerged from the recession.

The consumer is the main driver of the economy, and consumer spending has been weak, especially in the services sector which is labor intensive and dominated by small firms. The University of Michigan's Index of Consumer Sentiment has not made a robust recovery and only about one in 10 consumers think government policy is "good," an historically poor showing. Weak consumer spending translates into poor sales for small firms which in turn provide little incentive to order new inventories, expand firms and hire workers.

Business owners, like consumers, are also pessimistic and uncertain about the future. Consequently, they are unwilling to borrow money and spend on expansion, or hire new workers. With weak sales growth, few new workers and inventories are needed. NFIB's Index of Small Business Optimism (Index), a composite of 10 questions, had not managed to escape recession level readings since the recovery started in 2009. Currently at 91.4, the Index averaged 100 from 1973 to 2008, and in recoveries, the Index went as high as 108. Even today, 19 percent more owners expect the economy to be worse in six months than expect it to be better.[3] The net percent expecting higher real sales in the coming months is about zero, with as many expecting lower as expecting higher. A record high percent have no interest in borrowing money since they have no good use for it given their pessimism about future prospects and their uncertainty. The survey also asks owners to select one of 10 issues as their single most important problem operating their business. In the most recent survey, 21 percent of owners cited regulations, 19 percent taxes and 16 percent poor sales. Financing and inflation are tied with 2 percent of owners citing each as their most important problem.

In addition to the monthly economic trends survey, NFIB conducts a more extensive survey every four years where members are asked to rate the severity of 75 potential problems on a scale of 1 to 7, anchored by "Critical Problem" on one end and "Not a Problem" on the other. The 10 most severe problems for small-business owners assessed are: "Cost of Health Insurance," "Uncertainty over Economic Conditions," "Cost of Cost of Natural Gas, Propane, Gasoline, Diesel, Fuel Oil," "Uncertainty over Government Actions," "Unreasonable Government Regulations," "Federal Taxes on Business Income," "Tax Complexity," "Frequent Changes in Federal Tax Laws and Rules," "Property Taxes (real, inventory or personal property)" and "State Taxes on Business Income." This list of challenges is a good starting menu for addressing the question of how to help the small business sector and create jobs.

Small businesses are a major source of economic activity and job creation in the economy, but small businesses have struggled to recover from the recession. The "middle class" includes millions of small business owners who compete with each other for the business of consumers. And most of the 6 million employer firms provide tens of millions of jobs to "the middle class", people who want a job and want to earn a living. The best way to help the "middle class" or those who want to join it is to provide job opportunities in the private sector where they earn their way by producing value. Washington sets the tone: it controls the major prices, incentives, taxes, regulations and policies that impact decisions made in the private sector by consumers and business owners. Meaningful changes here can do much to get the great private sector job generating machine back in gear.

[1] An economy without population growth cannot have secular job growth. Given the culture of the economy (who can work, get educated etc.), once labor laws (such as minimum wage) and regulations

are established. There will be no meaningful job growth, just shifting jobs as new technologies and discoveries replace old ones. The small business sector is the “R&D” of the economy, where new ideas are tried and tested. Many fail, but provide millions of jobs and invaluable work experience in the process.

[2] NFIB has about 350,000 member firms and has collected basically the same economic and expectations data from a random sample of members since 1973. These data provide a meaningful time series of data on the small business sector through recessions and booms. Although not a scientific random sample of all small businesses, it is likely that NFIB members experience the same economic and policy shocks as its non-member peers experience. There are an estimated 6 million employer firms in the small business sector plus many single worker businesses.

[3] NFIB’s Small Business Economic Trends survey ask whether owners believe that business conditions will be better, the same, or worse in the next six months. The data is reported as a net percent; the percent reporting “better” minus the percent reporting “worse.” February’s data reported a net negative 19 percent of owners feeling the economy will be better than worse in the next six months.