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DECISIONS REGARDING FIXED ASSETS BY THE SMALL BUSINESS-IMPACT OF THE TAX REFORM ACT OF 1986

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ABSTRACT

Acquiring assets and financing this acquisition are important issues for the small business. This paper analyzes the present value of cash flows under lease and purchase options. A model is developed, which shows the impact of the 1986 Tax Reform Act on this decision. The critical value of the asset at the end of the lease term is mathematically determined. The optional Section 179 expensing election is also considered.

INTRODUCTION

Property, plant and equipment constitute a substantial portion of the assets of most small businesses. As these firms face the problem of allocating scarce economic resources, the means of acquiring and financing the acquisition of these fixed assets is very important. This paper will address the impact of the Tax Reform Act of 1986 in the determination of how to finance the cost of acquisition. The decision of whether to purchase or lease assets will be analyzed, focusing on the effect of any tax changes on the variables to be considered.

Several features of the Tax Reform Act of 1986 will impact this decision. Modifications in ACRS depreciation provisions and other changes are analyzed as to whether owning or renting an asset is optimal. Analysis of the tax effect requires the addition of another variable when discussing small businesses. Since many small businesses are owner-operated, especially in the early years, they may be organized as sole proprietorships. These will be taxed at differing rates from those organized as corporations. Our discussion must, therefore, include both variables, purchase versus lease the asset, as well as the legal form of the business.

In deciding whether to lease or purchase fixed assets, several aspects must be considered. Terms of the contracts may vary, but the typical advantages of leasing assets include the transference of ownership risks such as obsolescence to the lessor, avoidance of a sizable downpayment, possible less costly financing, possible flexible payment plans, and avoidance of the accompanying large liabilities associated with financing, i.e., "off-the-balance sheet financing." While these factors must be considered, we will focus on the financial issues, ascertaining the financial and tax impact of the decision.

Data for a hypothetical firm is developed, whereby the financial position and operating statistics are assumed, with the variables being the data generated by the decision to purchase or lease. For financial reporting purposes, it is assumed the provisions of the lease allow for treatment as an operating as opposed to capital lease. The lease payments are treated as rental expenses, no assets are capitalized, but more importantly, the business avoids recording the liability, which would adversely affect their financial ratios (off the balance sheet financing). For tax purposes, the annual payments required under the lease would normally be deductible as operating expenses, regardless of the accounting treatment accorded the agreement. A present value analysis differential cash flows is presented. MODEL SPECIFICATIONS AND ASSUMPTIONS

Radford Plastics needs a truck for transporting raw materials and finished products. Two avenues of acquisition are explored:

Purchase Outright

The acquisition cost, including sales tax, is $27,040. The downpayment required is 10% of the invoice cost plus the sales tax, totaling $3,690.48. The amount financed, $23,349.52, at 8% interest requires monthly payments of $570.03 over the next 48 months. The salvage value of the truck at the end of 4 years is anticipated to be $8,000.

Lease Contract (1)

Lease payments are set at $550 per month for the next 48 months. Should the company desire to purchase the asset at the end of the lease period, the fair market value of $8,000 must be paid, as there is no bargain purchase option in the lease contract.

A comparative cash analysis follows, developed for both alternatives. The monthly payment streams will be discounted on a monthly basis, at an annual rate of 8%. The tax savings with respect to each alternative are assumed to be realized at the end of Years 1-4, respectively. The acquisition occurred in January of 1987, therefore any tax calculations are using the schedules and rates under the Tax Reform Act of 1986. In Table II, Radford Plastics is assumed to be a corporation with taxable income less than $50,000. Table I provides the cash flow related to the two options, with related tax savings (at a 15% rate for the given income level): ________________________

(1) The terms of the lease require the lessee to assume all maintenance and other operating expenses of the truck. Full service leases were not explored, since the costs quoted were prohibitive.

TABLE I CASH FLOW DATA

Purchase Lease Downpayment $3,690.48 -- Monthly payments (48 months) 570.03 550.00 Residual Value: A.) If ownership is maintained -- 8,000.00 B.) If ownership is terminated <8,000.00> Tax Benefits: Depreciation Under ACRS: Year 1 (5408 x .15) < 811.20> Year 2 (8653 x .15) <1,297.97> Year 3 (5192 x .15) < 778.82> Year 4 (3115 x .15) < 467.25> Interest Expense: Year 1 (1,681.53 x .15) < 252.23> Year 2 (1,253.35 x .15) < 188.00> Year 3 (789.61 x .15) < 118.44> Year 4 (287.44 x .15) < 43.17> Rental Payments (6600 x .15) per year <990>

When discounted at an annual rate of 8%, the present values of these cash outflows for the respective years under both options are shown in Table II:

TABLE II PRESENT VALUES OF CASH FLOWS (15% TAX RATE)

Purchase Lease Year I $9,258.88 $5,406.13 II 4,790.57 5,002.68 III 4,903.10 4,632.16 IV 4,824.07 4,288.87 ----------------- ----------------- PV of Cash Flows $23,776.62 $19,329.84 Ownership Question: A.) Asset purchased at end of Lease 8,000 x .73503 -- 5,880.25 ----------------- ----------------- PV of Case A $23,776.62 $25,210.08 ----------------- ----------------- PV of Cash Flows $23,776.62 $19,329.84 B.) Asset ownership terminated (2) at end of Year 4 Loss of 1/2 Years Depreciation 171.72 (8000-265.50) x .73503 <5685.09> ----------------- ----------------- PV of Case B $18,263.25 $19,329.84 ____________________________ (2) If the asset is sold for $8000 at end of year 4 (Case B), the taxable gain is : $8000- [27.040 - (5408 + 8653 + 5192 + 1557)] $8,000 - 6230 = $1770, which allows for one-half years depreciation in the year of sale. Taxed at 15%, the tax is $265.50. Taxed at 28%, the tax is $495.60.

Based on the analysis of the present value of the cash outflows, excluding the residual value of the asset, the four years considered would favor leasing the asset. If the company determined ownership was beneficial at the end of Year 4, a further payment would be required under the leasing option. In this case, the present value of leasing payments exceeds the purchase option. If the company decided to terminate their ownership interest, the asset could be sold under the purchase option, resulting in an after tax cash inflow as shown. In this case, the present value of the cash outflows of the purchase option is also below the leasing alternative.

Based on this analysis, the decision is severely impacted by the value of the asset at the end of four years, since this variable changed the present values of the options. Given the assumptions of our model, we have mathematically determined the critical value of the truck at the end of four years to be $6,292.79. (3) If the truck is worth more than this value, purchasing minimizes the present value of future costs; if worth less, leasing is the better option.

Should the company be organized as a sole proprietorship, we have assumed a marginal tax rate of 28%. Table III shows the present values using this assumption. ________________________ (3) PV(purchase) + Loss of Depr - [SP - tax/rate (SP - BV] .73503 = PV(leasing) Benefits

TABLE III PRESENT VALUE OF CASH FLOWS (28% TAX RATE)

Purchase Lease Year I $ 8,405.50 $ 4,611.68 Year II 3,686.48 4,267.09 Year III 4,285.82 3,951.05 Year IV 4,498.99 3,658.21 -------------- -------------- PV of Cash Flows $20,876.79 $16,488.03 -------------- -------------- Ownership Question Case A - Purchase leased asset $ 5,880.24 -------------- PV of Case A $20,876.79 $22,368.27 -------------- ----

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PV of Cash Flows $20,876.79 $16,488.03 Case B - Asset sold Loss of 1/2 Years Depreciation 320.55 (8000 - 495.60) x .73503 <5,515.96> --------------- -------------- PV of Case B $15,515.96 $16,488.03 --------------- --------------

Using mathematical analysis (3), the critical value for the truck in this case is $6,475.79. This analysis is also applicable for corporations with taxable income in excess of $50,000, as the marginal tax rates are closer to 28% than 15%. (4) ________________________ (4) The Tax Rate for Corporations are as follows: Taxable Income Rate % 0-50,000 15 50,000-75,000 25 over 75,000 34

Optional Section 179 Expensing

Section 179 of the Tax Reform Act of 1986 would allow our taxpayer the option of expensing $10,000 in the year of purchasing the asset. The deduction of ACRS depreciation is then calculated on the reduced basis. Should this election be made, the following analysis pertains, assuming the 15% tax rate.

PV of Cash Flows if purchased from Table II $23,766.62 Tax Savings from Section 179 Expensing $10,000 x .15 x .92593 < 1,388.89> Reduced Depreciation Tax Savings Yr1: 2000 x .15 x .92593 277.78 Yr2: 3200 x .15 x .85734 411.52 Yr3: 1920 x .15 x .79383 228.62 Yr4: 1155 x .15 x .73503 127.34 ------------------- PV of Cash Flows $23,432.99 -------------------

The election of Section 179 expensing results in a $343.63 savings when calculated on a present value basis over the four year life. Since the present value of the cash outflows is still greater for purchasing than leasing, the decision will continue to be impacted by the residual value of the asset at the end of this period. A similar analysis using the 28% sole Proprietorship rate results in a PV of Cash Flows of $20,235.36 with a $651.43 savings.

Conclusions

The present value of cash outflows over the four years of the lease would favor leasing the asset. When the ownership issue is added to the analysis, the present values may change in favor of purchasing. Based on the assumptions of our model, we have determined a critical value, above which the decision would favor purchasing the asset, below which leasing is the better alternative.

This analysis focused on minimizing the present value of cash outflows, including tax benefits of deductible features of both plans. There may be other mitigating factors, the risk of obsolescence and level of inflation, which may contribute to a company's decision. In high technology industries, obsolescence may render the residual value very questionable; therefore, leasing may be the better alternative, with the risk being assumed by the lessor. All factors considered, the management of a small business must be aware of the alternatives available, including the tax implications of their decisions.

EXPORT FINANCE FACILITATION SERVICES ENABLING SMALL BUSINESS TO OVERCOME BARRIERS TO INTERNATIONAL TRADE

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ABSTRACT

Export finance services are provided by a variety of firms to facilitate international export trade. The focus of this study is to identify the range of export finance facilitation services offered to U.S. small businesses. Data were obtained using a questionnaire mailed to 550 U.S. export trading companies, export management companies and financial institutions. The data were compiled and statistically analyzed to define which services are being provided to U.S. small business and to what extent these services are being employed. The results indicate that although a variety of export financial services are offered, they are not fully utilized by U.S. small business.

STATEMENT OF PURPOSE

U.S. exports are responsible for maintaining one out of every nine manufacturing jobs and for generating one out of every seven dollars of total goods produced. Furthermore, the Department of Commerce estimates that nearly eighty percent of all U.S. exports are produced by less than one percent of the manufacturing firms in the United States. (1) Yet, while approximately 40,000 small to medium size manufacturing firms are capable of profitably producing goods for export, they are not engaging in such activity, due in large part to the existence of financial barriers to international trade. (2) Recognizing the increasing difficulty of U.S. small business to participate in international trade, and the significant economic benefits to be realized by focusing aggressively on expanding U.S. imports, the U.S. Senate Committee on Small Business surveyed small businesses in 1982 to identify the factors which presented barriers to export trade. The problems noted by the respondents included lack of information, regulation constraints, incursion of exorbitant expenses and problems in financing exports. The survey further revealed that the solution of various financing problems represented the greatest need. Specifically, the financial risk, cost of capital, difficulty in obtaining credit, inadequate capitalization, lack of income tax incentives, difficulty in obtaining payment for exports and other banking inefficiencies. (3)

In response to these findings, the U.S. Department of Commerce International Trade Administration (ITA) focused on marketing concerns and increasing the awareness of U.S. products in the international marketplace rather than on the financial issues identified by the U.S. Senate. In 1985, a study conducted for the California State World Trade Commission documented that very little has been accomplished to satisfy exporters' financing needs. (4) Therefore, the purpose of this study is to identify the efforts of export trading companies, export management companies and financial institutions to respond to the identified need for export finance facilitation services required by small U.S. export businesses.

METHODOLOGY

Sample Population

A questionnaire was mailed to 550 U.S. export trading companies, export management companies and financial institutions. Data were received from 69 respondents to this study defining their involvement in export payment facilitation services, production financing and/or credit facilitation services, reduction of export financing costs, international financial strategy management and financial risk management. (Appendix)

Respondent Characteristics

Two-thirds of those firms responding to this survey are physically located in the Eastern Standard Time Zone. Most of the respondents have provided export finance facilitation services to U.S. exporters for less than nine years. The median number of exporters serviced by the respondents is ten firms.

Nearly eighty percent of the respondents provide export finance services to firms exporting industrial products. Only thirty to forty percent of the firms surveyed provide export finance services to exporters of consumer products, agricultural products and/or services.

Three-fourths of the survey respondents required less than $100,000 of total exports before making a commitment to provide export finance facilitation services. The majority of those firms surveyed had 1985 revenues from export related services in 1985 of less than $500,000. However, thirty percent of the respondents had revenues from export related services of $1 million to $5 million.

Export finance services are provided to exporters whose products are shipped to the following geographic areas (listed in order of frequency): Western Europe, South America, Asian Pacific Rim, central America, Southeast Asia, North Africa/Middle East, Japan, Australia/New Zealand, Canada, South Africa, Africa (south of the Sahara) and Eastern Europe/U.S.S.R.

Eighty percent of the responding firms have less than five employees responsible for export finance activities. Prior export finance experience is the predominant prerequisite for hiring export finance personnel with less than thirty percent of the respondents employing personnel have a college degree.

One final characteristic of those firms surveyed, only ten percent were "certified" under the Export Trading Company Act of 1982.

FINDINGS

Export Payment Facilitation Services

Export payments are primarily facilitated through the use of letters of credit, with over seventy percent of the firms surveyed providing this service either directly or indirectly. A letter of credit is an instrument issued by a bank, whereby, the bank promises to pay a beneficiary (the exporter) upon presentation of certain "completion" documents specified in the letter of credit.

Standby letters of credit and accounts receivable collection services are also utilized to a great extent with approximately fifty percent of the firms surveyed providing these services either directly or indirectly.

Both private and government-sponsored credit insurance programs are used to a lesser degree. Of those programs in existence, the Foreign Credit Insurance Association (FCIA) programs are most widely used to facilitate export payments with approximately forty-five percent of the firms surveyed providing access to this service either directly or indirectly. The FCIA is a private association of approximately fifty leading U.S. insurance companies, affiliated with the Export- Import Bank, that provides short- and medium-term credit insurance to exporters, enabling them to obtain or offer better financing terms. FCIA policies insure payment for the export of such product as consumable products, small manufactured items, spare parts, raw materials and farm products.

Production Financing and/or Credit Facilitation Services

Most export financing is "transactional" in nature; production financing does not appear to be provided to any significant degree. Credit facilitation services provided are done so primarily through commercial banks with repayment terms of less than a one year. Over forty percent of the survey respondents provide access to commercial bank financing either directly or indirectly.

Longer-term credit facilitation services for periods of up to five years are made available through various Export-Import Bank loan programs, most notably of which is the Commercial Bank Guarantee Program. One-third of the survey respondents provide access to this program either directly or indirectly. Under this program, the exporter must self-finance the export transaction or obtain commercial bank financing; the Export-Import Bank (and/or FCIA) then guarantees repayment. Exports covered under this program include mining and refining equipment, construction equipment, agricultural equipment, general aviation equipment, manufacturing equipment and communications equipment.

Reduction of Cost of Capital

Exporters' cost of capital reductions are achieved primarily through the use of electronic funds transfer services and foreign exchange trading services. Forty percent of those firms surveyed provide these services either directly or indirectly. Cash management services, loan guarantees and factoring are all provided either directly or indirectly by less than 25% of those firms surveyed.

International Financial Strategy Management

International financial strategy management services focus mainly on currency decisions relative to an exporter's source of payment and/or source of borrowing. Between thirty and forty percent of the firms surveyed provide these services either directly or indirectly.

Very little support is provided to U.S. small business in evaluating importers' credit worthiness, implementing financial management control systems or selecting foreign financial institutions, with these services being provided by less than twenty-five percent of the respondents.

Risk Management

Foreign exchange trading and FCIA programs are utilized most frequently to manage U.S. exporters' financial risk, with thirty-five to forty percent of the firms surveyed providing these services either directly or indirectly. Financial market "hedge" strategies, pricing strategies, currency swaps, export credit swaps and parallel loans are made available to small business exporters to a significantly lesser degree with less than thirty percent of the respondents providing access to these services.

EXPORT FINANCE SERVICES AND THE FUTURE FOR SMALL U.S. EXPORTERS

Based upon the responses to the survey questionnaire, it is readily apparent that a broad spectrum of export finance services are not being fully utilized by, or made available to, small U.S. exporters. For example, in the area of export payment facilitation services, the use of Banker's Acceptances and factoring/forfaiting could be greatly increased. In addition, more private insurance and Overseas Private Investment Corporation programs could be undertaken, as well as an expansion of the Export-Import Bank-sponsored programs.

Small Business Administration financing programs were surprisingly under-utilized with only twenty percent of the survey respondents providing access to such loans.

Furthermore, the increased utilization of cost of capital reduction techniques and more sophisticated financial and risk management strategies should greatly impact the ability of the small U.S. exporter to efficiently and effectively compete in the international trade environment.

Finally, small U.S. exporters should consider expanding the formation of trade "cooperations" or "consortiums" in an effort to increase their accessibility to heretofore underutilized export finance services. To date, the existing trade "co-operatives" appear to focus primarily upon marketing strategies, whereas reducing the financial cost and risk of exporting has been identified as the greater need of today's small U.S. exporters.

FURTHER RESEARCH

This study has identified a variety of export finance services currently being provided by export trading companies, export management companies and financial institutions. Particular services are provided to a significantly greater degree than are other services. Thus, the question is raised as to whether those services provided most frequently are done so because they most effectively address the needs of small U.S. exporters or whether they are most cost effective for those firms providing such services. The answer to this question must be borne out by researching the specific export finance needs of small U.S. exporters. Such a research project is currently being conducted by the authors.

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APPENDIX Survey of Export Financing Facilitation Services

1. How long has your firm been in business? Median = 9 years

2. How many U.S. exporters are currently served by your firm? Median = 10 firms

3. In which "time" zone is your firm located?

Pacific 11.6% Mountain 21.7% Central -- Eastern 66.7%

4. If you would characterize your firm as an "Export Trading Company." is your firm certified under the Export Trading Company Act of 1982?

Yes 11.6% No 63.8% N/A 24.6% If no, why not? ____________________

5. What percentage of your annual revenues are derived by facilitating exports of:

0% 1%-25% 26%-50% 51%-75% 76%-100%

a. Industrial Products 21.7% 36.2% 7.2% 8.7% 26.1% b. Consumer Products 59.4% 29.0% 5.8% 1.4% 4.3% c. Agricultural Products 63.8% 20.3% 5.8% -- 10.1% d. Services 62.3% 24.6% 5.8% 2.9% 4.3% (For example: If your firm realizes 20% of its annual revenues by facilitating the export of agricultural products, check the column 1%-25%.)

6. To which of the following geographic areas does your firm facilitate exports (total should equal 100%):

0% 1%-25% 26%-50% 51%-75% 76%-100%

a. Canada 72.5% 24.5% 2.9% -- --

b. Mexico 68.1% 27.5% 1.4% 1.4% 1.4%

c. Central America 53.8% 40.6% 1.4% 1.4% 2.9%

d. South America 46.4% 43.5% 5.8% 2.9% 1.4%

e. Australia/ New Zealand 69.6% 29.0% -- 1.4% --

f. Asian Pacific Rim 52.2% 33.3% 4.3% 1.4% 8.7%

g. Japan 68.1% 23.2% 2.9% 4.3% 1.4%

h. Southeast Asia 59.4% 37.3% 1.4% -- 1.4%

i. Western Europe 44.9% 34.8% 11.6% 4.3% 4.3%

j. Eastern Europe/USSR 89.9% 8.7% -- -- 1.4%

k. N. Africa/Middle East 59.4% 30.4% 5.8% -- 4.3%

l. South Africa 85.5% 13.0% -- 1.4% --

m. Africa 87.0% 11.6% -- -- 1.4%

7. What were your gross revenues from export-related services in 1985?

a. Less than $250,000 37.7% e. $5,000,000-$10,000000 2.9%

b. $250,000-$500,000 14.5% f. $10,000,000-$25,000,000 --

c. $500,000-$1,000,000 15.9% g. $25,000,000-$100,000,000 --

d. $1,000,000-$5,000,000 29.0% h. More than $100,000,000 --

8. Which of the following export payment facilitation services does your firm provide or assist an exporter to obtain? Do Not Provide Provide Service Assist in Obtaining Service Directly Directly or Indirectly Directly Service or Indirectly

a. Letters of Credit 37.7% 34.8% 27.5%

b. Bankers' Acceptance 21.7% 15.9% 62.3%

c. Accounts Receivable 30.4% 14.5% 55.1% Collection

d. Electronic Fund Transfer 24.6% 18.8% 56.5%

e. Standby Letters of Credit 26.1% 21.7% 52.2%

f. Factoring/Forfaiting 10.1% 15.9% 73.9%

g. Credit Analysis of Importers 23.2% 18.8% 58.0%

h. Private Credit Insurance 13.0% 18.8% 68.1%

i. OPIC Insurance Programs 13.0% 13.0% 74.0%

j. FCIA Programs 18.8% 26.1% 55.1%

k. EXIM Bank Loans for Im- 17.4% 13.0% 69.6% porters of US Products

l. Other ____
____

9. Which of the following production financing and/or credit facilitation services does your firm provide or assist exporters to obtain?

Do Not Provide Provide Credit Assist in Obtaining Service Directly Directly Credit or Indirectly

a. Private Financing 1) Short-Term (1 yr.) 18.8% 15.9% 65.2% 2) Medium-Term (1-5 yrs) 4.3% 11.5% 84.1% 3) Long-Term (5-10 yrs) 2.9% 8.7% 88.4%

b. Commercial Bank Financing 1) Short-Term (1 yr.) 21.7% 20.3% 58.0% 2) Medium-Term(1-5 yrs) 11.6% 13.0%

75.4% 3) Long-Term (5-10 yrs) 7.2% 13.0% 79.7%

c. Government Sponsored Trade Financing 1) EXIM Bank Commer- cial Guarantee 13.0% 20.3% 66.75% 2) EXIM Bank Discount Loan Program 7.2% 18.8% 74.0%

d. Small Business Admini- stration 1) Working Capital Loans 8.7% 13.0% 78.3% 2) Contract Loans 5.8% 11.6% 82.6% 3) Seasonal Lines of Credit 7.2% 11.6% 81.2% 4) Export Revolving Lines 5.8% 15.9% 78.3% of Credit

e. Private Export Funding Cor- poration (PEFCO) Financing 2.9% 11.6% 85.5%

f. International Financing 1) World Bank Loans 5.8% 13.0% 81.2% 2) Inter-American Bank Loans 5.8% 13.0% 81.2% 3) African Development Bank 2.9% 8.7% 88.4% Loans 4) Asian Development Bank 2.9% 11.5% 85.5% Loans

g. Commodity Credit Corpora- tion (CCC) Loans 7.2% 10.18% 82.6%

h. Accounts Receivable Finan- cing 27.5% 13.0% 59.5%

i. Inventory Financing 21.7% 13.0% 65.2%

j. Lease Financing 10.1% 14.5% 75.4%

10. Which of the following services do you directly provide or facilitate with respect to reducing exporters' cost of capital?

Provide Provide Do Not Provide/ Directly Indirectly Facilitate Directly/Indirectly a. EXIM Bank Discount Loan Program 8.7% 14.5% 76.8%

b. Electronic Funds Transfer Services 20.3% 15.9% 63.8%

c. Foreign Exchange Trading Services 15.9% 15.9% 76.8%

d. Factoring/Forfaiting 8.7% 14.5% 69.6%

e. Loan Guarantee 15.9% 14.5% 69.6%

f. Cash Management Services 17.4% 13.0% 69.6%

g. Access to Foreign Credit Markets 2.9% 18.8% 78.3%

11. Which of the following international finance strategy management services do you provide:

Provide Provide Do Not Provide/ Directly Indirectly Facilitate Directly/Indirectly a. Capital Budgeting 5.8% 7.2% 87.0%

b. Foreign Professional Evaluation 15.9% 13.0% 71.0%

c. Financial Management Control Systems 10.1% 10.1% 79.7%

d. Foreign Financial Institution Selection 15.9% 10.1% 73.9%

e. Currency Decisions 1) Source of Payment 23.2% 17.4% 59.4% 2) Source of Borrowing 15.9% 14.5% 69.6%

12. Which of the following risk management services do you provide exporters directly or indirectly?

Provide Provide Do Not Provide/ Directly Indirectly Facilitate Directly/Indirectly

a. Foreign Exchange Trading 23.2% 13.0% 63.8%

b. Foreign Exchange Exposure Management 15.9% 13.0% 71.0%

c. Foreign Exchange Reporting/ Consolidation 13.0% 4.3% 82.6%

d. Foreign Credit Insurance 20.3% 20.3% 59.4% Association Insurance (FCIA)

e. Overseas Private Investment 8.7% 14.5% 76.8% Corporation Insurance (OPIC)

f. Forward Market Hedge Strategies 15.9% 4.3% 79.8%

g. Money Market Hedge Strategies 13.0% 4.3% 82.7%

h. Balance Sheet Hedge Strategies 8.7% 4.3% 87.0%

i. General Commodity/Service Pricing 5.8% 7.2% 87.0% Strategies

j. Currency Swaps 10.1% 10.1% 79.7%

k. Back to Back or Parallel Loans 8.7% 11.6% 79.7%

l. Export/Credit Swaps 5.8% 13.0% 81.2%

13. a. Does your firm assist in the development and implementation of Foreign Sales Corporation? 24.6% Yes 73.9% No

b. If yes, do you perform the work "in-house" or utilize "outside" services (i.e., attorneys or accountants)? 15.9% In-house 17.4% Outside Services

14. How does your firm price its services? ______________________________________

____

15. What dollar value of exports does your firm require/forecast for a product/service before it is willing to commit its export financing facilitation resources to a U.S. supplier?

a. Less than $100,000 72.5% d. $500,00-$1,000,000 7.2%

b. $100,000-$250,000 7.2% e. $1,000,000-$5,000,000 4.3%

c. $250,000-$500,000 5.8% f. More than $5,000,000 2.9%

16. How many persons are employed by your firm, who specifically handle export financing matters?

a. Less than 5 81.2% d. 25-50 1.5%

b. 5-15 13.0% e. 50-100 ---

c. 15-25 4.3% f. More than 100 ---

17. What criteria do you emphasize when selecting an employee for your firm whose primary responsibility is/will be export financing facilitation?

a. Mostly Experience 40.6%

b. Experience and High School 1.4%

c. Experience and College Degree 27.5%

d. Experience and Post-Graduate Degree 14.5%

e. Other (specify) ____________________ 14.5%

18. a. Does your firm employ "country" experts Yes 37.7% No 62.3%

b. If yes, do they speak the language of that country? Yes 39.1% No 60.9%

c. How many such experts does your firm employ? Median = 1

d. To what degree are your "country experts" familiar with the unique import financing requirements specific to their country of expertise?

Very Familiar 4.3% Somewhat Familiar 1.4% Not Familiar 94.3% (or no response)

FINANCIAL REPORTING AND DISCLOSURE A CONTINUING PROBLEM FOR SMALL BUSINESSES

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ABSTRACT

Small businesses continue to be faced with financial reporting and disclosure problems caused by the need to generate financial statements in conformance with generally accepted accounting principles (GAAP). This paper reviews the Big GAAP-Little GAAP controversy, identifies areas where disclosure is a problem, and discusses options available to the Financial Accounting Standards Board in dealing with small businesses. Managers of small businesses need to be aware of financial reporting services provided by CPAs, such as audits, reviews, and compilations.

How do GAAP and other comprehensive basis of accounting relate to these reporting options?

A BRIEF HISTORY

Generally accepted accounting principles (GAAP) consist of the rules, procedures, and practices utilized in financial statement preparation and presentation. From 1939 to 1959 Accounting Research Bulletins were issued by the AICPA's Committee on Accounting Procedure dealing with a wide array of accounting topics. In 1959 the AICPA replaced the Committee on Accounting Procedure with a part-time Accounting Principles Board that was charged with the responsibility, of developing accounting principles and bringing consistency to the profession. The Financial Accounting Standards Board (FASB), consisting of seven full-time members, replaced the Accounting Principles Board in 1973 and has been active in the promulgation of accounting principles from that date to the present. Today, it is commonly recognized the three most influential forces in structuring accounting principles practices are the FASB, the Securities and Exchange Commission, and the American Institute of Certified Public Accountants.

Throughout history, regardless of the promulgating board, a concerted effort was made to develop principles that would be applicable to financial statements of all firms, large and small and publicly or privately held. The result of board actions, however, was a proliferation of accounting standards leading to accusations that pronouncements were oriented toward large businesses and ignored the needs of small companies. Owners and managers of small businesses complained that accounting costs were too high and that information contained in financial statements was lacking in usefulness. Rule 202 of the AICPA Code of Professional Ethics does not allow for differentiation in generally accepted auditing standards due to client size except where GAAP specifies financial reporting exemptions for non-public entities [3]. Consequently, CPA firms tended to encourage complete adherence to GAAP for all clients.

As a result of the above conditions some CPAS, small business executives, and others began to push for a separate set of generally accepted accounting principles to be developed for small businesses. In response to the pressure for a "Little GAAP" various groups including the American Institute of Certified Public Accountants and the Financial Accounting Standards Board appointed committees and conducted research relating to this problem. Research results have been identified and discussed by other authors. Nair and Rittenberg identified four AICPA committee reports and discussed the report of the Technical Issues Committee of the AICPA Private Companies Practice Section [17]. Jefcoat and Loudell [7] and Lippitt and Oliver [13], explained the recommendations of the AICPA Committee on Generally Accepted Accounting Principles for Smaller and/or Closely Held Businesses and the AICPA Committee on Small and Medium Sized Firms. In addition, Lippitt and Oliver reviewed the preliminary results of a survey sponsored by the FASB and the University of Florida [15]. Knutson and Wichmann also addressed the Report of the AICPA Committee on Generally Accepted Accounting Principles for Smaller and/or Closely Held Businesses as well as the Report of the Standards Overload Committee [9]. Finally, Korn discussed a study by the Financial Executives Research Foundation [11]. Table 1 lists the various reports by year and highlights significant items from the articles mentioned above.

TABLE 1

SUMMARY OF REPORTS RELATING TO APPLICATIONS OF GAAP TO SMALL BUSINESS

Year Report or Study Highlights

1976 Report of AICPA Committee on Gener- * Identified two problem areas - measure- ally Accepted Accounting Princi- ment and disclosure. ples for Smaller and/or Closely * Opposed different measurement proc- Held Businesses esses for small businesses. * Contended the measurement process should be independent of the nature of the users.

1980 Report of AICPA Committee on Small * Concluded that some of the measurement and Medium Sized Firms standards required by GAAP lacked eco- nomical justification or were not useful for small companies. * Recommended the FASB review GAAP applicability to small business and study effects of standards on small business before issuance.

1982 Survey by FASB and the University * Indicated small CPA firms, small busi- of Florida nesses, and bankers were not suppor- tive of a separate set of accounting standards for small businesses.

1982 Sunset Review Committee - Techni- * Completed review of GAAP to identify cal Issues Report from the Private measurement and disclosure require- Companies Practice Section Divi- ments not relevant to small and medium sion of CPA Firms size private companies or that required costs in excess of benefits provided.

1983 Report of Standards Overload Com * Recommended reconsideration of costly mittee of AICPA and/or burdensome disclosure require- ments. * Encouraged simplicity of new rules or principles. * Preliminary report recommended consid- eration of income tax basis for mail businesses (alternate to GAAP).

1982 Study by the Financial Executives * Supported one set of GAAP for all size 1983 Research Foundation firms, but was receptive to different disclosure rules due to size and nature of the entity.

BIG GAAP - LITTLE GAAP CONTROVERSY

In addition to the extensive studies identified in Table 1, numerous articles have been written addressing the merits and problems of a separate GAAP for small businesses or exploring other possible alternatives. Stanga and Tiller [21], Lippitt and Oliver [16], Knutson and Wichmann [10], Nair and Rittenberg [18], Korn [12], Friedlob and Plewa [6], Anderson, Dycus, and Welker [4], and Jefcoat and Loudell [8] have all identified and discussed arguments for and against separate accounting principles for small businesses. Table 2 consists of a compilation of arguments favoring and opposing a separate GAAP for small businesses selected primarily from the articles mentioned above.

The cost of accounting services to small businesses relative to the benefit derived has been and continues to be an area of concern. A study conducted by Nair and Rittenberg found the banking community, business community, and CPAs all perceive that compliance with present accounting regulations is costly [19]. Benefits are not only difficult to identify but also to a large extent accrue to third party users. Costs, however, are readily identifiable and continue to increase. Factors pressuring costs upward include: (1) the need of the CPA to conform to Generally Accepted Auditing Standards (GAAS) and to determine that financial statements are in conformity with GAAP to avoid professional sanctions or litigation, (2) the need for CPA firms to undergo peer review that could easily cost $2500 to $3000, and (3) rapidly increasing liability insurance costs to CPAs that will be passed on to clients through higher fees.

In spite of costs and a general belief that disclosure requirements are too stringent for small companies, there appears to be insufficient support to force the establishment of a separate set of GAAP for small businesses. Financial statement users find comfort in knowing that statements are prepared in conformance with some universally applied principles. CPAS, while recognizing the need for relief for small businesses, are reluctant to dilute the standards of the profession and lose credibility. They are, therefore, more likely to support one set of GAAP and hope the Financial Accounting Standards Board will exempt small companies from certain disclosure requirements.

TABLE 2

ARGUMENTS FOR AND AGAINST A SEPARATE SET OF GAAP FOR SMALL BUSINESS

Arguments For

* GAAP are written primarily for users of financial statements of public companies, not small non-public entities. * Small companies find GAAP costly to apply relative to the benefits. * GAAP often deals with complicated situations

that do not apply or only partially apply to smaller companies. * Investors in large businesses and small businesses view the financial statements from a different perspective. * Small business owners have access to substantial amounts of internal information making detailed disclosures less important. * CPAs do not believe that disclosure requirements are equally applicable for large and small companies, or for privately owned and publicly owned companies. * User needs differ between small closely held businesses and large publicly held companies. * The Financial Accounting Standards Board is oriented toward large corporations. * Accounting standards which are numerous and detailed appear threatening to small business owners who often do not have a professional accounting staff.

Arguments Against

* Two sets of GAAP will tend to reduce credibility and cause confusion among statement users. One set would be looked upon as inferior. * The financial information needs of creditors are similar for small closely held companies and large public companies. * While there is a desire for relief from current standards for small business, preparers and users are reluctant to recommend separate GAAP for small and large companies. CPAS, bankers and businessmen tend to support uniform principles. * From a legal viewpoint form is more important than size in determining rights and obligations. * Separate sets of GAAP would have an adverse effect on consistency and the comparability of large and small businesses would be hindered. * Defining small business is difficult and determining who should use which set of GAAP would be controversial. * Companies in the same industry should be applying the same GAAP. * A common set of standards is necessary to insure quality and integrity in the accounting profession. * There are substantial similarities in the business processes of all firms.

DISCLOSURE PROBLEM AREAS

Financial reporting and disclosure problems for small businesses fall into two general areas or categories, measurement and disclosure. In 1976, the AICPA Committee on Generally Accepted Accounting Principles for Smaller and/or Closely Held Businesses concluded that measurement rules must be applied across the board but that disclosure standards may be unnecessarily burdensome to small businesses [14]. In recent years the Financial Accounting Standards Board has shown a willingness to reduce some of the disclosure requirements for non-public companies. This is exemplified by no longer requiring earnings per share or segmental disclosures for privately held companies.

According to Williams and Thompson there are nine topical areas that currently cause reporting and disclosure problems for small business clients of CPA firms. They are:

1. Irregular Income Items 2. Reporting Changes in Financial Position 3. Interperiod Income Tax Allocation 4. Leases by Lessees 5. Commitments and Contingencies 6. Marketable Securities 7. Related Party Transactions 8. Subsequent Events 9. Problems of Continued Existence [221

The above list consists of topics covered in professional development courses for CPAs that are common to small businesses; therefore, it is unlikely disclosure requirements relating to them will be suspended or reduced.

ALTERNATIVES

In view of standards overload and the reporting and disclosure problems confronting small businesses, what options are available? The Standards Overload Committee identified five possible alternatives as reported by Nair and Rittenberg [20]. They are: (1) retain the status quo, (2) develop a separate set of GAAP for small, private businesses, (3) simplify GAAP, (4) change the auditor's reporting standards, thus, encouraging special reports with fewer required disclosures, and (5) use a comprehensive basis of accounting (OCBOA) other than GAAP.

It is highly unlikely the FASB will consider either numbers two or three above; it has, in fact, indicated a preference for retaining GAAP as is and allowing some suspensions of disclosure requirements. Alternative 5 is already in use.

Given the current reporting options available to small businesses, it does seem that no new alternatives are actually needed. Following is a range of reports that are available to small public and/or private companies relating to reporting and disclosure requirements: (1) an audit that meets SEC requirements (public companies), (2) an audit for non-public companies, (3) a review, (4) a compilation with disclosures, (5) a compilation without disclosures, (6) other comprehensive basis of accounting, and (7) financial forecasts. Users of financial reports will likely request statements with full disclosures as long as they don't have to pay for them. Management of small businesses should, therefore, become aware of accounting services such as reviews, compilations, and other comprehensive basis of accounting and be prepared to negotiate a lower level, less costly report with users.

REPORT OPTIONS

Three reporting options are generally available to small businesses; audits, reviews, and compilations. A look at the definitions of these options, will better allow us to understand the differences between the options. Auditing is the process by which a competent, independent person accumulates and evaluates evidence about quantifiable information related to a specific economic entity for the purpose of determining and reporting on the degree of correspondence between the quantifiable information and established criteria [5]. The established criteria is better known as generally accepted accounting principles (GAAP) or in a few cases some other comprehensive basis of accounting. The outcome of an audit is the expression of an opinion or disclaimer of opinion regarding the fairness of presentation of the financial statements in conformity with GAAP. A review of financial statements involves performing inquiry and analytical procedures that provide the accountant with a reasonable basis for expressing limited assurance that there are no material modifications that should be made to the statements in order for them to be in conformity with generally accepted accounting principles or if applicable, with another comprehensive basis of accounting [1]. A compilation of financial statements is limited to presenting in the form of financial statements, information that is the representation of management (owners) without undertaking to express any assurance on the statements [2]. From these definitions we can determine the primary purpose of each of the reporting options: (1) audits, to determine if the financial statements are fairly presented in conformity with GAAP or in a relatively few cases some other comprehensive basis of accounting, (2) reviews, to determine if modifications are needed to conform with GAAP, and (3) compilation, to generate financial statements.

REPORT POSSIBILITIES

What are the different report possibilities under the three reporting options? Under the audit three different opinions are possible; unqualified, qualified, and adverse, along with the possibility of issuing a disclaimer of opinion. An unqualified opinion will be used when the auditor was able to conduct the audit in accordance with generally accepted auditing standards and found the financial statements fairly presented in conformity with GAAP and consistently applied with prior years. A qualified opinion is used when the financial statements as a whole are fairly presented but there is a problem somewhere within the statements; this problem may be caused by GAAP departures, GAAP disclosures, consistencies, and uncertainties. An adverse opinion will be issued when the financial statements are not fairly presented. Adverse opinions are caused by GAAP problems, some of which could be the same as those which cause a qualified opinion, except that to be adverse the GAAP problem must be more material. There are only two situations which lead to a disclaimer of opinion. Causes of a disclaimer are when the auditor is unable to determine if the financial statements are fairly presented or materially misstated and if the auditors independence is impaired. The standard review report will be used if no material adjustments are needed for the reports to be in conformity with GAAP. Alterations in the standard review report will be required for such items as inadequate disclosures required by GAAP or departures from GAAP. Compilation reports give no assurance regarding the fairness of the financial statements. The standard compilation report will be issued in most situations. However, modifications to the standard wording may be necessary in the following situations: departures from GAAP, substantially all disclosures are omitted, a comprehensive basis of accounting other than GAAP was used in preparation of the financial statements, and the CPA was not independent.

ADVANTAGES AND DISADVANTAGES OF REPORTING OPTIONS

The primary advantage of an audit is found in the opinion of the auditor relating to the fair presentation or lack of fair presentation of the financial statements. The assurances provided in the audit report are valuable in communicating with stockholders, bonding agencies, bondholders, and other third party creditors. A disadvantage of the audit is its relative expensiveness in comparison with the other reporting options. Advantages of the review option are its lower cost compared to an audit, and limited assurance that no material modifications are needed for conformity with GAAP, which makes them more desirable to creditors and stockholders, and increases usefulness to management. Compilations provide a very valuable service to the small business sector, which many times does not have the expertise on board to generate adequate financial statements. The cost of a compilation report is the lowest of the three alternatives. One major disadvantage of the compilation is the lack of any assurances on the part of the accountant.

OTHER COMPREHENSIVE BASIS OF ACCOUNTING

Much attention is given to at least the following three comprehensive basis of accounting: (1) strict cash basis, (2) modified cash basis, and (3) income tax basis. The strict cash basis of accounting recognizes revenue when cash is collected and expenses when cash is disbursed, with no capitalization of fixed assets or recognition of receivables or liabilities. A modified cash basis also recognizes revenue when cash is collected and expenses when cash is disbursed, however, it does capitalize fixed assets and may allow for the recognition of receivables and payables. Probably the most intriguing of the three is the income tax basis. This method allows a business to use the same accounting methods for income tax filing and for financial reporting. The advantages would be reduced accounting costs and elimination of time consuming and difficult adjustments. How would these three comprehensive basis relate to our three reporting services: (1) audits, (2) reviews, and (3) compilations? Statement on Auditing Standards #14 allows a CPA to express an opinion on financial statements prepared under some other comprehensive basis than GAAP. This type of reporting is considered a Special Report and may cause additional risk for the auditor. The review of financial statements does not allow for reporting under a comprehensive basis of accounting other than GAAP, since it only applies to GAAP or statements that require a material modification to be in conformity with GAAP. The compilation does allow for reporting under a comprehensive basis other than GAAP but it does require modification of the wording in the standard report. Remember that our discussion earlier indicated that the CPA does not give any type of assurance when he issues a compilation report, therefore the compilation report may not meet the needs of the business.

SUMMARY

Much has been written over the years regarding BIG GAAP vs. LITTLE GAAP. These discussions may range from allowing different accounting methods and different accounting principles, to alternative comprehensive basis of accounting for large and small businesses. Although strong arguments can be brought forward for allowing small businesses special concessions in the area of financial reporting, it is our feeling that the controversy will continue in the future with one single GAAP prevailing, due to the benefits of comparability, understanding, and uniformity.

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FOUR CRITICAL FINANCIAL TECHNIQUES FOR SMALL BUSINESS

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ABSTRACT

Because net cash flow and net profit are not synonymous terms for many cash-poor smaller firms, its CEO must forecast cashflows, compute the cash breakeven point, forecast the balance sheet, and calculate the firm's sustainable growth rate.

INTRODUCTION

One reason that a small business is not a "little big business" is that the forecasted cash flow for many small businesses will not equal forecasted net profit plus depreciation. Relative resource poverty has been cited by numerous small business theorists as a major characteristic distinguishing smaller from larger firms. Because the small firm lacks sufficient cash and that which cash can purchase, effective financial decision-making processes within the small company are especially critical. The small business manager who uses income and expense values to forecast cash receipts and disbursements may reduce the life chances of the firm. Four essential financial techniques which operationalize the distinction between profit and cash are described: cash flow forecasting, cash breakeven, balance sheet forecasting, and sustainable growth rate. The use of each assists the small business manager in estimating future cash needs and thus avoid the dangers and disadvantages of eleventh-hour attempts to cover cash deficits.

CASH FLOW FORECASTING

Cash flow forecasting describes the anticipated movement of cash during the year. Preparation of a cash flow forecast or budget requires the construction of a worksheet that lists month by month all expected cash receipts and all expected cash disbursements. Net cash flow is the difference between cash receipts and cash disbursements. This worksheet, rather than a monthly projection of revenues and expenses, is of paramount importance to the small firm because its managers cannot assume that net profit calculated under accrual accounting rules will equal net cash flow, or that in the short run net profit plus depreciation will equal cash flow. Thus, a small resource- poor firm's chances of remaining in business depend on net cash flow and not on its net profit. Despite the critical importance of the distinction between cash flow and net profit and the importance of cash budgets, researchers (2;4) report that only thirty percent of small firms prepare cash forecasts. Welsh and White (9, pp. 19-27; 10, pp. 33-70 and 77-93; 11, pp. 18-32; 12, pp. 222-259) have made the major contribution to the small business literature with their explication of the negative consequences that may accrue to a small firm whose managers use income, expense, and net profit analysis as proxy for cash receipts, cash disbursements, and net cash flow. Negative cash flow may coexist with positive net profit for several reasons. There may be timing differences in the cash receipts/cash disbursement cycles. This may occur, e.g., when the firm's average accounts receivable collection period exceeds its average accounts payable payment period. Projected income statements constructed under accrual accounting rules will not reveal the potential danger for a small firm caught between thirty-day supplier terms and slow-pay/ no- pay customers. Other causes of cash flow/net profit divergence during a year are: inventory buildup, salary and tax payment cycles, business seasonality, and the disbursement of cash for non-expensible transactions, e.g., the payback of debt principal to a bank. As will be demonstrated below, rapid growth is a major cause of a divergence between net profit and cash flow. The small business must use cash flow forecasting to ascertain both the dollar amount and the precise timing of negative cash flow since it, unlike larger firms, cannot assume that additional debt and/or equity will be automatically forthcoming to cover a temporary cash shortage. The identification of cash deficit problems through cash flow forecasting is the first step in developing an effective cash management strategy, involving, e.g., inventory and accounts receivable control. As Welsh and White (10, pp. 98-104) demonstrate, cash flow forecasting may also challenge, in certain circumstances, the conventional wisdom of recommending that a firm always take supplier cash discounts, even to the extent of borrowing to take those discounts.

CASH BREAKEVEN

While the conventional breakeven computation (total fixed costs divided by the contribution margin ratio) is quite helpful to the smaller firm in determining whether there is enough profit potential in a product or service, it should not be used to answer the question of whether cash receipts will equal cash disbursements at a given level of sales. If it is used to estimate future cash needs, it may lead the firm into future liquidity problems, since a comfortable projected safety margin (the amount by which projected dollar sales exceed conventional breakeven sales) may coexist with a projected negative net cash flow. Thus, to estimate the dollar amount of future cash needs, the smaller firm must compute the cash breakeven point (CBEP)(l): ________________________________ (1) This formula is a modified version of that provided in an article (1) provided by Brian Belt.

CBEP = TFC(l-T) - NCET + CTNE --------------------------------- CMR (1 - T) where:

TFC = total fixed costs T = proportional income tax rate (federal, state, local) NCET = non-cash expense transactions, i.e., those expense transactions not involving cash disbursements (e.g., depreciation, bad debt expense) CTNE = non-expensible cash transactions, i.e., those cash disbursements not involving expansible items (e.g., repayment of debt principal to a bank) CMR = the contribution margin ratio (the percentage of each sales dollar left, after covering total variable costs, to apply to fixed costs and profit).

All of the values used in the formula are forecasted ones. The formula assumes positive taxable income and that all sales are cash sales. Belt (1) provides adjustments to account for lags in sales receipts collections and lags in cash disbursements for expenses (including accounts payable). He also provides a cash breakeven formula for the on-going firm. Cash breakeven is defined as the forecasted dollar sales level at which cash receipts will equal cash disbursements, i.e., the forecasted sales level at which no net cash loss will occur. if the CTNE value exceeds the NCET one, the cash breakeven point will exceed the conventional breakeven point at a given level of forecasted sales and the firm could face a net cash loss at the same time it projects a positive net income. The presumption is that foreknowledge of this eventuality is advantageous. This is not an unlikely scenario since small firms carry proportionally more debt (and a higher level of current debt to total debt) than larger firms, and hold only thirty-seven percent of total assets in long-term assets compared to sixty percent for larger firms (7, pp. 183-211).

An Example

Assume that a firm forecasts for next year net sales of $1,370,000, with total variable costs (TVC) of $959,000 and total fixed costs (TFC) of $348,000. Depreciation will be $125,000 and return of debt principal will be $225,000. The firm's contribution margin ratio (CMR) is 0.3, and the conventional breakeven sales amount is $1,160,000. Since forecasted sales exceed the breakeven amount by $210,000, the firm's executives may be led astray unless they calculate the firm's cash breakeven sales level. With a projected net profit of $63,000, assume a total tax rate of ten percent. Thus, a check (cash out) must be written for $6,300.

CBE = TFC (1-T) - NCET + CTNE --------------------------------- CMR (1-T)

CBE = $348,000 (1 - .10) - -----------------------

$125,000 + $225,000 -------------------------- .3 (1 - .10)

= $413,200 ----------- .27

CBE = $1,530,370

Since the cash breakeven sales level exceeds the conventional one, the firm's executives should compute the net cash gain or loss with sales at the forecasted level of $1,370,000.

CASH IN $1,370,000

CASH OUT TVC ($1,370,000 x .70) $959,000 TFC ($348,000-$125,000) 223,000 CTNE 225,000 TAX ($63,000 x-10) = 6,300 --------------- TOTAL CASH OUT $1,413,300 ---------------

The net cash loss over the year associated with the forecasted net profit of $63,000 is $43,300. Net profit does not equal net cash flow for this small firm.

Use of the cash breakeven formula will not pinpoint the exact time during the course of a year that a cash loss will occur, nor the magnitude of that loss. It reveals only the size of the net cash loss (a sum of all cash losses and cash gains) at the end of the forecasted year. Thus, while valuable for gross sensitivity analyses, it is clearly no substitute for month-by-month cash flow forecasting.

FORECASTING THE BALANCE SHEET

The firm employs current and fixed assets to create sales. As the firm's sales level grows, additional assets are required. Thus, a firm must forecast its balance sheet to determine the dollar amount that must be invested in additional assets and to plan the source of the dollars (debt and/or equity). Again, the presumption is that it is to the firm's advantage to plan. The steps in forecasting the balance sheet are: 1) identify each asset and liability that varies directly with sales. These are variable assets (VA) and variable liabilities (VL); 2) relate the dollar amount of each VA and each VL to past sales levels, e.g., cash may be running historically at 2% of sales, inventory at 15%, etc.; 3) apply the historical ratio derived in step 2 for each VA and VL to the forecasted dollar sales level to derive the forecasted dollar amount for each VA and VL and extend these dollar amounts on the pro forma balance sheet; 4) calculate the forecasted net worth by adding forecasted net profit to and subtracting forecasted dividends from the previous (last year's) net worth; 5) compute the magnitude of the financial gap, i.e., the amount of new debt and/or equity required to make the balance sheet balance. (2) Again, this forecasting technique addresses the size of the potential shortfall, not its precise timing. ________________________ (2) These steps are based on Duryee and Enger (3, pp. 47-51). The authors provide a formula which uses the historical dollar total of all variable assets (TVA) divided by sales and the historical dollar total of all variable liabilities (TVL) divided by sales. The formula is:

$TVA X Dollar increase - $TVL ------- in sales -------- Sales Sales

X Dollar increase in sales - Net income

+ Dividends = New debt and/or equity required.

In the example: .3915 x $136,400 - .0017 x $136,400 - $41,000 + 0 = $10,804

0.3915 is $267,000 divided by $682,000; .0017 is $8,000 divided by $682,000.

An Example

Balance Sheet - December 31, 1986

ASSETS SVA/SALES Cash $148,000 (.2170) Accounts Receivable 54,000 (.0792) Inventory 22,000 (.0323) Other Current 43,000 (.0630) Fixed 595,000 ------------ TOTAL $862,000

LIABILITIES & EQUITY SVL/SALES Current Liabilities $ 8,000 (0-0117)

Long-term 484,000 Total Liabilities 792,000 Stockholder's Equity 370,000 ------------ TOTAL $862,000

1986 net sales were $682,000 with net income of $34,000. Assume that the historical relationship to sales of the variable assets and liabilities are represented by the values in parentheses ($VA divided by SALES) in the Balance Sheet above, e.g., cash has historically run at about .2170 of net sales. Assume forecasted 1987 sales are $818,400 and forecasted net income is $41,000 with no dividend payout contemplated. The entries for the December 31, 1987 pro forma Balance Sheet would be derived as follows:

ASSETS Cash $177,593 ($818,400 x .2170) Accounts Receivable $ 64,817 ($818,400 x .0792) Inventory $ 26,434 ($818,400 x .0323) Other Current $ 51,559 ($818,400 x .0630) Fixed $595,000 ------------- Total Assets $915,403

LIABILITIES & EQUITY Current Liabilities $ 9,575 ($818,400 x .0117) Long-term Liabilities 484,000 Stockholders' Equity 411,000 ------------ Subtotal $904,575 Financial Gap 10,828 ------------- Total $915,403

SUSTAINABLE GROWTH RATE

Growth is a two-edged sword and the edge facing the smaller, resource-poor firm is razor sharp. Because growth requires the disbursement of cash for additional assets, a small firm can grow itself broke. Computation of the firm's sustainable growth rate (SGR) enables the firm to address in trade-off form the question of how fast the firm can grow in sales without experiencing cash problems. The formula from Higgins (6) is as follows:

SGR = P (l - D) (I + L) ---------------------- T- [P (1 - D)(l + L)]

where :

P = the ratio of net profit (after tax) to net sales D = the ratio of dividends to net profit (after tax) L = the ratio of debt (total liabilities) to equity T - the ratio of total assets to net sales.

An Example

Assume that the firm's after tax net profit ratio is four percent, the dividend payout ratio is twenty percent, the debt-to-equity ratio is two hundred fifty percent and the asset to sales ratio is fifty- five percent.

SGR = .04(1 - .20)(1 + 2.50) ------------------------------ .55-[.04 (1 - .20)(I + 2.50)]

= 25-57 percent

If the firm has these historical, targeted, or mandated (e.g., D and/or L mandated by bank) ratio values and the CEO cannot or will not inject additional equity, there is only one rate at which sales can increase, i.e., 25.57 percent. The firm can grow safely at this rate without changing its operating efficiency (P, T) or financial strategy (L, D). If managers and creditors operate under an inflation illusion, uniform inflation will reduce the nominal sustainable growth rate point for point (5). If the firm attempts to grow faster than this rate and does not change one or more of the P, D, L, T values and/or inject new equity, it will experience a cash crisis and may grow itself broke. Thus the firm should compute its SGR and seek to solve any liquidity problems before they occur. One option is, of course, for the firm to set its target growth rate equal to that which it can sustain, rather than change P, D, L, T and/or inject new equity. A similar version of this computation has appeared in an article by Ulrich and Arlow (8).

CONCLUSION

A critical success factor for the cash-poor smaller firm is a CEO who can "run the numbers." Because net cash flow and net profit are not synonymous terms for many small firms, the CEO wearing his/her treasury specialist hat, must forecast cash flows, compute the cash breakeven point, forecast the balance sheet, and calculate the firm's sustainable growth rate. If the small business CEO were forced to choose between income statements and cash flow statements for planning and/or control purposes, he/she must choose the latter. The big business manager's reliance on income and expense budgets alone to forecast cash needs should not be emulated. The CEO in the small firm must choose cash analysis because net profit does not equal cash.

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THE IMPACT OF LIABILITY INSURANCE ON SMALL BUSINESS

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ABSTRACT

Increases in liability insurance costs has affected all business in the United States. Small business has been especially impacted. This study investigated the impact of liability insurance costs on small business. A telephone interview survey was used to contact 165 small businesses in Cape Girardeau, Missouri. The results of the survey indicates that about 75% of the small businesses have experienced an increase in insurance premiums in the last 24 months. The businesses dealt with these increases by decreasing their insurance coverage 57% of the time and by passing the increased costs on to customers 21% of the time.

INTRODUCTION

While the insurance situation affects all businesses, the small business operator is especially prone to feel the effects of rising insurance premiums. This study was completed to better understand the impact of liability insurance on small business. The sample in this study consisted of small businesses in Cape Girardeau, the commercial hub for southeast Missouri. Three research questions were investigated:

1. What percent of small businesses have experienced premium rate changes in liability insurance in the last two years? 2. Of small businesses experiencing increased liability premiums, in what ways have the businesses dealt with these changes? 3. Do owners of small businesses feel there is a liability problem among small businesses at the present time?

Appropriate demographic characteristics of the respondents are included. In total 165 small businesses were contacted in the phone survey.

RELATED INFORMATION

The coverage provided by liability insurance is essential to many small businesses. However, there is a rising concern over the increasing costs of maintaining adequate liability coverage in the last ten years. These increased costs may be directly related to the increases in liability suits. Between 1977 and 1982, the number of civil law suits in state courts grew four times faster than the population in the United States. In the period between 1974 and 1984 the number of product- liability suits in federal courts increased 680% (5). The average verdit today in product liability suits is over one million dollars (9).

The present insurance situation is affecting businesses in different ways. Many larger businesses can absorb the rising costs of insurance. Smaller firms cannot absorb these costs as easily and have responded by decreasing or eliminating their product liability coverage in many instances.

A fundamental reason for this present situation with liability insurance is the stated losses insurers have taken due to increased liability awards (7). The insurers attribute the problem to lawyers fees and court awards. Lawyers attribute the situation to big business negligence. Big business is observing a change in the general publics willingness to bring suits. The result of all this finger pointing is unmanageable costs that small business must pay to receive insurance coverage. Not only are small businesses having difficulty in covering the costs, sometimes their liability insurance coverage is even cancelled (3).

There appears to be a concentration of large law suits in certain areas of the United States. New York, California, and Florida are the top three states that have awarded multi-million dollar settlements (4). Certain states are acting to limit certain liability awards. In Missouri there is a 350,000 dollar cap for non-economic loss in liability cases, yet wages and medical expenses are not capped (10).

Many small businesses are being affected by the present insurance situation. A representation of these effects will be provided. Most U.S. ski lift equipment manufacturers had their insurance cancelled or significantly increased due to the accident at Colorado's Keystone Resort in 1985 (5). In response to this accident there was a significant increase in the price of daily lift tickets.

Small trucking, bus lines, and city subway systems are all affected by the increasing costs of liability insurance. The American Public Transit Association reports premium increases of 300% to 1,200% in the last couple of years for bus and subway operators (12). The Southern California Rapid Transit District nearly shut down when its annual premium rose from $67,000 to $3.2 million (3). The American Trucking Association reports more than 100 companies have collapsed and more are expected to fail due to increased insurance costs.

Insurance companies are raising premiums for bars, restaurants, and liquor retailers. A restaurant in Concord, New Hampshire, protested a premium hike from $1,000 to $12,000 per year by sponsoring an Unhappy Hour of dramatically increased drink prices (3). Bismark Food Services, which sells beer at Detroit Tiger Stadium, had a premium of $50,000 in 1983 which increased to $1 million in 1986 (3).

Nationwide day care centers are facing a significant liability insurance problem. Because of widely reported cases of child abuse and molestation, the cost of insurance for day cares has risen significantly from 1980 to 1984. The average cost of insurance has risen from $7 to $70 per child. Additionally, liability insurance has been cancelled for more than 17% of child care centers nationwide (7).

Some groups significantly affected by the insurance crises are in the medical professions. Insurance premiums for oral surgeons in Detroit has risen about 200 percent in the last two years. A typical neurosurgeon on Long Island had premium increases in 1985 of $66,000 to $100,000 (12). The hardest hit group of the medical professions may be in the field of obstetrics. Coverage for obstetricians now runs up to $72,000 per year resulting in many refusing to deliver babies (3).

To conclude, no business has escaped the rising costs of today's insurance coverage. Some businesses have experienced over 500% increases in premiums in recent years. This insurance situation has caused many small businesses to decrease liability coverage, lower their profits, or discontinue operation of their business.

METHODOLOGY

A telephone interview survey was used to contact 165 small businesses in the Cape Girardeau area of southeast Missouri. These small businesses were chosen from over 1,000 businesses registered with the Finance Department in Cape Girardeau. A systematic random sampling procedure was utilized to identify the sample group.

The attitude survey included both demographic and liability insurance content questions. In order to assess the content validity of the survey it was screened by 16 semi-professionals and pretested with two local businesses, one retailer and one service provider. Their suggestions were used in the final revisions of the survey.

Descriptive statistics including percentages were used to describe the demographic characteristics. The chi-square test of independence was utilized to measure the relationship among the categorical independent variables (i.e., location, business focus, years in business, after-tax profits) and dependent variable which was their feeling of the existence of liability problems for small business today.

RESULTS

The demographics of the survey reported in Table 1 indicate that 41% of the respondents have been in business three years or less, while 57% have been in business 13 years or more. An approximate equal number of service and retail goods businesses were represented. Ninety-three percent of the businesses do carry some liability insurance while 74% of the businesses have experienced a change in insurance premiums in the last 24 months. Approximately 96% of insurance premium changes resulted in increases in insurance costs. About 57% of the businesses experiencing an increase dealt with it by decreasing their insurance coverage while 21% passed the costs on to customers. Only 15% of the businesses have experienced a liability claim against them in the last five years. A majority, 66%, felt that there is a problem with liability insurance costs with their business industry.

The chi-square test of significance was used to measure the association among categorical independent and dependent variables. The results of the chi-square tests are provided in Table 1. Three variables provide results of interest for the reader. Change in insurance cost in the last 24 months indicated a significant relationship with the dependent variable at the .0004 level. Additionally, the occurrence of a liability claim against the respondents business in the last five years also produced results at the .04 significance level. The variable, type of change, provided a chi-square significance of .07 which should be additionally considered.

TABLE 1 CHI-SQUARE TEST OF ASSOCIATION AMONG CATEGORICAL INDEPENDENT VARIABLES AND THE DEPENDENT VARIABLE (FEELINGS OF LIABILITY PROBLEMS WITH THEIR BUSINESS INDUSTRY)

Variable Alternative Percentage (%) Years in Business in Cape (n) (%) 0 - 3 41 27 x(2) = 3.90 4 - 6 24 15 df = 4 7 - 9 16 10 Significance = .42 10 - 12 14 8 13 Plus 57 40

Business Focus - Services (n) (%) Financial 14 18 x(2) = 2.38 Professional 3 3 df = 4 Home, Auto 21 25 Significance = .67 Beauty, Personal 12 15 Other 30 39

Business Focus - Goods (n) (%) Home, Office, Gift 16 19 x(2) = 2.47 Auto 16 19 df = 4 Food, Drug 13 16 Significance = .65 Clothing, Sporting 10 13 Other 29 33

Does Business Carry Liability Insurance (n) (%) Yes 140 93 x(2) = 1.39 No 11 7 df = 1 Significance = .40

Change in Insurance Cost in Last 24 Months (n) (%) Yes 108 74 x(2) = 12.39 No 39 26 df = 1 Significance = .0004

Type of Change (n) (%) Increase 105 96 x(2) = 3.17 Decrease 4 4 df = 1 Significance = .07

How Was Increased Insurance Cost Dealt With (n) (%) Passed Cost to Customers 21 20 x(2) = 2.07 Decreased Liability Coverage 57 53 df = 4 Changed Insurance Company 13 12 Significance = .72 Self Insured 6 6 Other 10 9

Has There Been a Liability Claim Against Your Business in the Last Five Years (n) (%) Yes 23 15 x(2) = 4.27 No 127 85 df = 1 Significance = .04

Do You Feel There is a Problem With Liability Insurance Costs With Your Business Industry (n) (%) Yes 100 66 No 52 34

What Is Your Approximate After-Tax Profit (n) (%) 0 - 25,000 32 30 x(2) = 1.32 25,001 - 50,000 39 35 df = 2 Over 50,000 40 36 Significance = .52

DISCUSSION

Based on the empirical data presented, certain conclusions can be drawn with respect to the attitudes of small business operators in Cape Girardeau, Missouri toward business liability concerns. The data suggests that the certain demographics of Cape Girardeau small businesses, i.e., years in business, business focus-services, business focus-goods, businesses carrying liability insurance, and how increased insurance costs were dealt with, were not significantly related to small business operators feelings about the existence of a problem with liability insurance costs within their business industry.

The independent variables that contributed the most to feelings of a problem with liability costs within certain industries were as follows: those businesses that had changes in their insurance costs in the last 24 months, those which experienced increases in insurance costs, and those businesses having a liability claim against them in the last five years.

While the feelings by small businesses of problems with liability insurance appears to be most closely related to increasing liability insurance costs or liability claims, which appears logical, how these small businesses are dealing with increased liability insurance costs should be more closely reviewed. Over one-half (57%) of the small businesses dealt with these increased costs by decreasing liability coverage. An additional six percent decided to self-insure which may be interpreted as dropping liability insurance coverage. Only 21 percent of the businesses contacted in the study indicated they passed the increased costs on to their customers. The fact that over one-half of the small businesses sampled decreased or eliminated liability insurance coverage creates a concern related to the perceived lack of legal protection for many small businesses if liability claims were filed against them.

The results of this study should be evaluated in relationship to its limitations. The major limitation to be considered is the generalizability of these results beyond the sampled population. Even given this limitation the results may be very beneficial to the small business community.

Additional studies that looked at responses from small businesses that are demographically representative of the overall national population may be useful to small businesses in their decisions regarding liability insurance. The comparison of the differences between different types of business, i.e., goods and services, may also be very beneficial.

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THE IMPORTANCE OF WORKING CAPITAL IN THE FINANCING OF CURRENT ASSETS

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ABSTRACT

A questionnaire study was conducted to find out the Montana business managers use of the working capital concept. Perceptions of the business manager regarding the following questions were explored:

1. the lender's willingness to finance current asset requirements on both a short-term and a long- term basis; 2. the present financing of current assets; 3. the proper financing of current assets; and 4. the relative importance in borrowing of repayment history, net worth, profit, and cash flow.

The majority of the Montana business firms round it difficult to obtain long-term credit financing for even a portion of current assets, and are apparently unaware of the working capital concept.

BACKGROUND OF STUDY

Working capital is current assets (cash, receivables, inventory, etc.) minus current liabilities (debt obligations due within one year). Working capital may also be viewed as the amount of a business's current assets provided (financed) by long-term debt and/or equity.

If, for example, a business has no current liabilities, working capital equals current assets. In the situation just described, 100% of current assets are provided (financed) through long-term debt and/or equity. If, in contrast, a business has exactly $0 working capital, current assets equals current liabilities. Or, in other words, 100% of current assets are provided (financed) with short- term debt (current liabilities).

A business that has no working capital or very little working capital will likely have difficulty in paying short-term debt obligations from operational sources of cash in sustained or sudden declines in sales. Therefore, the importance of maintaining an appropriate level of working capital and its contribution to business survival is a concept that small business managers should understand. Managers should develop a working capital philosophy that they can apply and monitor carefully.

THE STUDY

The study was conducted to find out the Montana business managers use of the working capital concept. Perceptions of the business manager regarding the following questions were explored:

1. the lender's willingness to finance current asset requirements on both a short-term and a long- term basis; 2. the present financing of current assets; 3. the proper financing of current assets; and 4. the relative importance in borrowing of repayment history, net worth, profit, and cash flow.

A questionnaire was sent to 175 Montana retail businesses. The majority of the 175 businesses were sole proprietorships and partnerships. The 175 businesses were randomly selected from the State of Montana, Department of Commerce list of 1,500 Montana businesses. Eleven questions were asked.

Two mailings were sent. The second mailing was sent to those not responding to the first mailing. No statistical difference, at the .05 level, was found between the replies of the two groups. Therefore, one may be statistically confident that the survey sample was representative of Montana businesses.

Thirty-four percent of those surveyed replied to the mailed questionnaire. Ten percent of the returned questionnaires were incomplete and not usable; 30 percent of those sent (53 questionnaires) were used in this analysis.

Business Size and Number of Years in Business

The majority of the respondents were small businesses with only 19 percent having annual sales of over $1 million. The median sales of the respondents was $50,000 to $300,000. Approximately 90 percent of the business firms had been in business over five years. None of the businesses had been in business for less than a year. The respondent businesses are the survivors of several poor business years in Montana.

Lender Willingness to Finance Current Assets

The latitude business managers have in applying business working capital philosophies may be constrained by lenders. Are lenders willing to grant loans on current assets on both a short-term and long-term basis? Can the business firms adjust their working capital position to meet business objectives, i.e., profitability at an acceptable level of risk? An aggressive financing approach requires less working capital (CA-CL) than a more conservative financing approach which requires more working capital.

When asked, "To what extent are financial institutions willing to finance your business needs for cash, inventories, and accounts receivable through short-term loans (less than one year in duration)?", on a scale from 1 (very little) to 5 (a great deal), approximately 45.3 percent answered 5 (a great deal). When asked, "To what extent are financial institutions willing to finance some of your business needs for cash, inventories and accounts receivable through long-term loans (greater than one year in duration)?", only 29.4 percent answered 5 (a great deal). Thus, a number of managers perceive it is difficult to obtain long-term financing for even a portion of current assets. As a result, many small businesses may be forced into a risky short-term debt position.

How are Current Assets Financed?

Fortunately, the majority of businesses appear to have a high percentage of current assets financed by long-term debt and equity rather than short-term debt. Approximately 62 percent had 30 percent or less of the current assets financed by short-term debt. The current asset needs of 88.7 percent of the businesses fluctuated up to 40 percent over a four year time period.

How Should Current Assets be Financed?

In answering the question, "Should some of your current assets be financed by long-term debt and ownership investments?", answers were as follows: yes - 26.9 percent, no - 36.5 percent, and doesn't matter - 36.5 percent. Thus, a majority of the respondents are apparently unaware of the working capital concept (an aggressive approach versus a conservation approach - profits versus risks). It is also possible that some of the businesses are 100 percent equity financed and would be indifferent for that reason.

Do Current Asset Needs Fluctuate?

Current asset needs typically fluctuate over a time period. A conservative approach dictates that the permanent portion of current assets should be financed through long-term debt or equity. An aggressive approach would dictate short-term financing. On the question, "How much do current asset needs fluctuate over a four year time period?", the answers were, respectively, 0 to 20 percent - 47.2 percent; 21 to 40 percent - 41.5 percent; 41 to 60 percent - 7.5 percent; and 60 to 80 percent - 3.8 percent. Thus, current asset needs of the respondents vary over time indicating that many small businesses probably have a temporary portion of peak current assets.

What is the Importance of Certain Criteria in Granting Current Asset Loans?

On a scale of 1 (little importance) to 10 (very important), respondents were asked to rank the importance of repayment history, net worth, profit, and cash flow in receiving short-term credit.

Approximately 55 percent ranked repayment history and net worth a 10 (very important). Approximately 15 and 20 percent ranked profit and cash flow, respectively, a 10 (very important). Apparently, the ability to repay short-term loans with cash flow from operations is not as important to lenders as the business firm's net worth. Net worth can be severely eroded from a collapse in real estate and farm land values. When this erosion of values occurs, bankers may then look at cash flow and refuse to roll over short-term loans.

Comments by Respondents

Respondents were asked to give their comments about the causes of the credit crisis in Montana (if they believed there is one). Comments were as follows:

1. Recent business failures have caused banks to be in a very conservative posture.

2. Inexperienced business managers fail to use supplier financing to its fullest advantage. Sometimes merchandise can be bought ahead of season with significant price breaks without a change in the payment due date.

3. Sales have decreased markedly every year since 1980.

4. No crisis exists for reasonable and profitable ventures.

5. Banks are bottom-line oriented and not interested in their communities any more.

6. The economy is in the worst shape in over 20 years in most of the state. Bank loan officers with experience are few and far between - good ones having left the field. These factors have caused very conservative attitudes to prevail and unwillingness and inability to assist customers who are in financial trouble.

7. Lenders do not see the importance of small business success to the overall economy.

8. Our personal credit crisis was increased from the lack of any financial institution allowing any line of credit from our beginning. One note, no matter how small or large, had to be paid in full before any extra credit was allowed. There was no fluctuating credit for the different levels of volume of business during the year. This did not allow us to have the right amount of merchandise at the right time of year.

9. In general, I think people have trouble in getting credit because of those who have abused the privilege and because institutions (whether financial, insurance or whatever) tend to have these standardized forms and try to put people, with a few similar characteristics, into broad categories for "rating purposes" instead of analyzing each one individually -- which may seem unrealistic -- but it might be more equitable in the long term.

10. There is definitely a credit crisis in Montana, our local bank will not do anything. We need a long-term repayment type loan to be able to survive the bad economy.

11. We were forced to find a smaller bank and they have been very helpful - very objective with advice.

12. Inexperienced, irresponsible loan officers unable to judge the values of assets used for collateral or viability of a business are a big part of the problem. Banks can lead you down the road to failure.

13. Banks seem to be hesitant (to lend money) because they don't understand some of these businesses and can't make an educated decision.

The comments indicate there is a credit "crisis" in Montana. Better education for both the lender and borrower is necessary, particularly in the financing of working capital.

SUMMARY

The importance of working capital is quite often overlooked by both the borrower and the lender. Working capital may be viewed as the amount of a business's current assets financed by long-term debt and/or equity. A business that has little or no working capital is likely going to have difficulty in paying or refinancing short-term debt during times of business declines which may be accompanied by a tightening of business credit.

The majority of business firms in this study find it difficult to obtain long-term credit financing for even a portion of current assets, and are apparently unaware of the working capital concept.

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INTERSTATE BANKING AND SMALL BUSINESS

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ABSTRACT

The banking industry is poised on the edge of a major wave of mergers. The legal barriers which have prevented interstate banking and allowed over 14,000 banks to operate independently are crumbling. In most western industrial countries, the banking industry is highly concentrated. This paper reviews the movement towards interstate banking and its potential impact on small businesses. The results of a survey of small business people in Tompkins County, New York and their attitudes toward local vs. non-local banks are analyzed, and implications for the merger trend are discussed.

INTRODUCTION

The 1980s have been the decade of deregulation. The airline industry, the telecommunications industry and the banking industry have all undergone or are in the process of undergoing deregulation. What makes the deregulation of banking interesting is the industry's long history of strict regulation and the concern by some that while the deregulation of airlines and telecommunication increased competition by spawning new firms, the deregulation of banking will decrease competition. Numerous commentators in the popular press and scholarly journals have predicted a substantial decline from the 14,000 plus commercial banks in the U.S. today. Haegele and Poje (4), for example, predict that over half of the banks in business today will be eliminated through acquisition, merger or liquidation as a result of deregulation and the spread of interstate banking. This implies an increase in the concentration of economic power and a decrease in competition in the banking industry. This paper will review the movement towards interstate banking and discuss its potential impact on small businesses. The results of a survey of small business people and their attitudes toward local versus non-local banks will be analyzed and implications for the merger trend will be discussed.

HISTORY

The current regulatory environment for controlling interstate banking is determined by the MacFadden Act of 1927 and the Douglas Amendment to the Bank Holding Company Act of 1956. The MacFadden Act limits branching by national banks to their home state subject to any additional restrictions determined by the states. Illinois, for example, had very restrictive branching regulations which made Continental Illinois highly dependent on volatile purchase money to fund its growth rather than more stable retail deposits. This hastened Continental's decline when problems arose in its loan portfolio. The Douglas Amendment to the Bank Holding Company Act of 1956 also limits geographic expansion by forbidding a bank holding company from acquiring banks in another state unless state authorities approve the acquisition. As a result of these restrictions, over 14,000 commercial banks, from the very large money center banks to small community banks, do business in the U.S. today. In most Western industrial countries the banking industry is populated by far fewer but far larger banks. The historical restrictions on interstate banking were never a complete barrier to geographic expansion of banking activities across state lines. Banks could offer bank services across state lines so long as commercial lending and deposit functions were separated. Edge Act Corporations, designed to promote financing of international trade and increase American competitiveness in international banking, allowed banks to establish out-of-state facilities. The Garn-St. Germain Depository Institutions Act of 1982 allowed banks and savings and loans to acquire failed institutions across state lines. Paul Volcker, Federal Reserve Board chairman, in testimony to Congress, reported that "U.S. bank holding companies in 1982 had 202 loan production offices and 143 internationally-oriented Edge Act corporations operating outside the parent's home state..."and "There are probably more today." (10)

The underlying impetus for the quickening interest in interstate banking comes not so much from forces within the banking industry but from the need in recent years for the banking industry to compete with the financial services companies such as American Express, Merrill Lynch, Prudential Bache and Sears. These firms offer many traditional banking services and more across state lines without being banks. Bankers fear that the financial services companies may preempt them in certain markets. The banking industry, especially larger banks, have openly lobbied regulators and politicians for deregulation and increased opportunities for interstate banking.

The regulatory trend today is in the direction of a banking system with virtually unrestricted interstate banking. The states are leading the movement in this direction. The first intermediate steps are the so-called regional compacts where cooperating states allow interstate banking within the designated region. Eventually, if the trend continues, the banking regulations of all states may resemble Maine's which permit and encourage within its borders banking services by local as well as non-Maine banks.

POTENTIAL IMPACT ON SMALL BUSINESS

If unrestricted interstate banking represents the future, what will be its impact on small businesses? The major concern by opponents of interstate banking and advocates of small business is the concentration of economic power in a community by a large bank able to buy out or drive out competitors through unfair competition. The eventual concentration of economic power might result in higher loan rates and more expensive bank services especially for smaller businesses. Large firms have other sources of funds, e.g., the bond market and commercial paper market, unavailable to smaller firms. (3,5)

Supporters of interstate banking attack the concentration of power and declining competition argument on several grounds. Competition in banking services comes today not only from banks, but also from very large financial services companies. Secondly, Douglass (2) reports that where big banks have been able to expand into new geographic areas, small well-managed locally owned banks have been effective competitors. Sohn (9), in a review of studies investigating bank size and economies of scale, supports Douglass' argument because economies of scale diminish in banks beyond $75 million in deposits. Finally, Nadler (6) challenges the conventional wisdom that deregulation of banking will lead to fewer banks. He supports his argument with the interesting fact that despite the deregulation process, there are almost 2,000 more banks today than 10 years ago.

In Maine, interstate banking with reciprocating states has been in effect since 1975 and unrestricted interstate banking since 1984. Those local institutions that chose to remain independent have grown at a faster rate since 1984 than before. Cocheo (1) reports that local bank officers are confident that they can compete with out-of-town rivals and continue to service their small business clients.

ANALYSIS

Given the trend towards unrestricted interstate banking, local businesses in Tompkins County, New York were surveyed during the summer of 1985 to determine their preferences for local versus non-local banks in order to understand the local business person's perception of some of the issues surrounding interstate banking. It should be noted that non-local banks in Tompkins County are all New York State banks that have either acquired local banks, e.g., Norstar or began their own branches here, e.g., Marine Midland. Local banks are predominantly owned by Tompkins County residents .376 firms were sampled. 46 percent (174) responded. Larger manufacturers, e.g., NCR, NYSEG, and Therm, Inc., not-for-profit institutions, government affiliated establishments and all banking institutions were excluded. 32 percent of the responding firms were in professional services, 26 percent in retail trade, 10 percent in food services, 4 percent in manufacturing and the remaining 28 percent in all other types of business. Table A shows mean and median statistics for a few characteristics of the sampled firms.

TABLE A: SAMPLE CHARACTERISTICS

	MEAN	MEDIAN
Annual Sales	$1,551,000	$500,000
Employees	29	8
Age of Business	27	20
Age of Respondents	45	45
Years business with same bank	17	15

The key variable that was examined in the survey was the attitude change that would occur if a local bank was acquired by a non-local institution, i.e., would the business person's confidence in the bank increase, decrease or remain unchanged. The small business person's attitude was examined rather than behavior (e.g., would an out of town acquisition provoke switching banks) because too many other variables such as existing loan agreements, interest rates, costs associated with switching banks, etc. might affect behavior. The small business person's attitudinal change may be a good predictor of future behavioral change.

Survey results indicated that only 10% of respondents would expect an increase in confidence if their institutions were acquired by a non-local institution. A majority (62%) would have a decline in confidence (see Table B).When asked to comment directly on an open ended question on the likelihood of changing banks if their local bank were acquired by an out-of-town bank (as opposed to commenting on confidence levels), 38% of the useable responses were classified as negative, 35% positive and 27% maybe.

Crosstabulation results when respondents are divided into quartiles indicate that a decrease in confidence when contemplating an out-of-town acquisition of a local bank is more likely to occur in larger small businesses than the very small (See Table C). Professionals (doctors, lawyers, accountants) are more likely to have less confidence in non-local banks (See Table D). Businesses which are older and have been doing business for more years with the same bank are more likely to have less confidence (See Table E&F). Those who have a predisposition to believe local ownership is an important criteria for choosing a bank will have a major decline in confidence if their banking institution is acquired. (See Table G).

TABLE B CHANGE IN CONFIDENCE LEVEL WHEN LOCAL BANK ACQUIRED BY NON-LOCAL BANK

Confidence Level Percent Cumulative Percent

Increase Very Much 2.4 2.4 Increase Somewhat 7.9 10.3 Remain Unchanged 27.9 38.2 Decrease Somewhat 40.0 78.2 Decrease Very Much 21.8 100.0

TABLE C SIZE OF BUSINESS (SALES $) AND CHANGE IN CONFIDENCE LEVEL

Sales ($) Confidence Remain Confidence (000s) Increases The Same Decreases % % %

Less than 250 8.8 38.0 52.9 250-499 6.3 40.1 53.1 500-1,499 11.4 14.3 74.3 Over 1,500 9.8 19.5 70.7

TABLE D TYPE OF BUSINESS AND CHANGE IN CONFIDENCE LEVEL

Confidence Remain Confidence Increases The Same Decreases % % % Retail 6.7 35.6 57.8 Mfg. 0 50.0 50.0 Professional 13.2 20.8 66.0 Food Service 17.6 35.3 47.1 Other 9.1 25.0 66.0

TABLE E NUMBER OF YEARS WITH PRESENT BANK AND CHANGE IN CONFIDENCE LEVEL

Confidence Remain Confidence Increases The Same Decreases Years % % %

0-4 9.8 29.3 61.0 5-14 10.8 40.5 48.6 15-25 14.3 40.5 61.9 Over 25 7.5 15.0 77.6

TABLE F AGE OF BUSINESS AND CHANGE IN CONFIDENCE LEVEL

Confidence Remain Confidence Increases The Same Decreases Years % % %

0-9 7.3 43.9 48.8 10-19 11.1 25.0 63.9 20-34 11.4 17.1 71.4 over 34 9.3 25.6 65.1

TABLE G IMPORTANCE OF LOCAL OWNERSHIP IN CHOOSING A BANK AND A CHANGE IN CONFIDENCE LEVEL

Confidence Remain Confidence Increases The Same Decreases % % %

Very Important 3.5 12.3 84.0 Important 5.4 30.4 64.3 Unimportant 14.7 50.0 35.3 Very Unimportant 43.7 31.3 25.0

SUMMARY AND CONCLUSIONS

Each week the financial press contains new stories about the spread of interstate banking. The historical restrictions on interstate banking may have served a national purpose of maintaining a more competitive, less concentrated, less powerful banking industry in local markets. Today, with the technology that exists in banking and related financial services, there are no local, independent markets. The restrictions on interstate banking have become anti-competitive restrictions that limit the choices that small businesses have for banking and financial services. The small business is better served by a more competitive banking industry.

This research shows, however, that a small independent community bank has a marketing advantage and should survive the elimination of interstate banking restrictions if the bank chooses to remain independent. Small businesses prefer doing business with local institutions. Other research (8) has shown that interest rates and full service are the most important factors that determine why a small business chooses a bank. The local bank that can adequately compete on rates and service should be able to keep its small business clientele because of their preference and confidence in local ownership.

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HOW TO DETERMINE YOUR NEEDS FOR AN EXPORT LICENSE

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ABSTRACT

The purpose of this presentation is to identify the issues involved in export licensing and the government agencies involved in the enforcement activities. Once the structure of the Federal Government's Export Licensing Program is understood, than requirements for making a Licensing Application can be discussed. Next the procedures that are followed after a license application has been submitted will be covered. Included in the material will be the different types of licenses that are available. The local Small Business Institute Director should have enough information to work on cases dealing with small businesses wanting and needing help in export licensing.

The major thrust of this report will be to provide a basic understanding of how our government's export licensing program works. The approach will have a "Hands On" emphasis to give the practitioner an easy guide line to follow. A sample application form will be included in the presentation.

INTRODUCTION Historical Development

Since before World War II export controls have been in affect. It was anticipated that as soon as the supply shortages created by the war were corrected the controls would be lifted. Because of the "Cold War" the Export Control Act of 1949 was passed. It provided for the continued use of controls to monitor exports to the U.S.S.R. and other communist countries that might have same military significance. It remained in effect for 20 years, being amended and extended as needed. On January 1, 1970 the act was replaced by the Export Administration Act passed in 1969. This was followed by the 1979 Act with the same name, which was amended in 1981. When the act expired on March 30, 1984. The Commerce Department's authority was extended under the International Emergency Economic Powers Act and continued indefinitely by Executive order 12470 of March 30, 1984 (49 FR 1 3099, April 3, 1984). In 1985 the Export Administration Amendments Act was passed and signed into law by the President. The basic intent of this act was to speed up and simplify the processing and application procedures. The role of the Defense Department was strengthened under the act.

The objectives for export control were identifies in the 1979 Export Administration Act. It authorized control over exports for the following:

1) Restrict exports that would make a significant contribution to the military potential of other countries to the detriment of U.S. national security.

2) Further significantly U.S. foreign policy or to fulfill declared U.S. international obligations and

3) Protect the domestic economy from the excessive drain of scarce materials and to reduce the serious inflationary impact of foreign demand

National security considerations currently outweight those of foreign policy short supply in importance for control purposes.

THE EXPORT TRADE ADMINISTRATION

The Office of Export Trade Administration (OEA) is part of the Department of Commerce's International Trade Administration. It has seven operating divisions. They are Policy Planning, Operations, Exporter Assistance, Computer Services, Foreign Availability, and Capital Goods and Production Materials, Scientific and Electronic Equipment. Planning Develops overall policies on export licensing and coordinates the involvement with other agencies. The operational division processes, reviews, and issues export licenses. Providing informational material to businesses and other government agencies through bulletins and federal Register announcements is the responsibility of the Export assistance division.

The enforcement function for violations of the regulations are primarily the responsibility of the Office of Export

Enforcement. The Office of Antiboycott Compliance does cooperate with them when restrictive trade practices or boycott issues are involved.

FIGURE 1 identifies the channels of command with three levels of management between the Director and the Under Secretary for International Trade. It also indicates that there is a Deputy Assistant Secretary for Export Enforcement to whom the Offices of Export Enforcement and Antiboycott Compliance report.

EXPORT ADMINISTRATION REGULATIONS

Information on the rules and regulation for export control are provide by the Department of Commerce in a publication titled "U.S. EXPORT ADMINISTRATION REGULATIONS". It should be considered one of the essential purchases for anyone interested in exporting. It is also used as a required text in any of the introductory or advanced courses which the Office of Export Administration offers.

This manual is updated periodically to reflect amendment and changes to the 1979 Act. For this reason it is important to maintain a current copy. The publication presents the regulations as they are titled in the 1979 Act. Once you have subscribed the bulletins and updates are provide, until a next edition is published.

Section one is an introduction which gives an overview of how to use the material. The remaining sections and topics are as follows:

Part 368 U.S. Import Certificate and Delivery Verification Procedure.

Part 369 Restrictive Trade Practices or Boycotts.

Part 370 Export Licensing General Policy and Related Information.

Part 371 General Licenses.

Part 372 Individual Validated Licenses and Amendments.

Part 373 Special Licensing Procedures.

Part 374 Reexports.

Part 375 Documentation requirements.

Part 376 Special Commodity Policies and Provisions.

Part 377 Short Supply Controls and Monitoring.

Part 378 Special Nuclear Controls.

Part 379 Technical Data.

Part 380-384 Are not included in the manual.

Part 385 Special Country Policies and Provisions.

Part 386 Export Clearance.

Part 387 Enforcement.

Part 388 Administrative Proceedings.

Part 389 Appeals.

Part 390 General Orders.

Part 391-398 Are not included in the manual.

Part 399 Commodity Control List.

The final section contains a sample of all the existing forms.

DETERMINING LICENSING REQUIREMENTS

FIGURE 2 graphically demonstrates the process and identifies the relevant "Parts" of the manual that need to be checked to determine the requirements.

By first checking the commodity control list (Part 399) you will encounter two listings an ECCN" number and a "PROC CODE". The ECCN is the Export Control Commodity number. FIGURE 3 is a sample page. There are 10 categories for grouping products. The first digit identifies the level of strategic control; the group code to which the commodity belongs is the second number and the last two digits are used to identify related products with in the grouping. This four digit number is followed by a code letter. The code letter is important in determining the documentation requirements from Part 375. The "PROC CODE" that accompanies the ECCN number is used for internal processing and routing of export licensing applications. Both of these must be included on your application form or it will prolong the application process. These numbers do not relate to the SIC or schedule "B" numbering systems.

Once the ECCN and POC CODE numbers have been obtained from Part 399 you can turn to Parts 371 and 379 to determine the type of license which is needed. This also leads you to use Part 385 which identifies the special country groupings, for government policy purposes. They are subject to change but currently are as follows:

Group Z: North Korea, Vietnam, Cambodia and Cuba.

Group Q, W and Y: U.S.S.R., and other Warsaw Pact Countries, Albania, Mongolian People's Republic, and Laos.

Group T: North, Central, and South America, Bermuda, and the Caribbean, except Cuba and Canada.

Group V: All countries not included in any other country grouping except Canada, which is not in any group.

TYPES OF LICENSES

Validated licenses are covered under Part 372 and are issued to authorize a specific export. There are five major licensing categories which are:

1) Individual License, which authorizes the export of technical data or quantities of commodities during a specified period to a designated cosignee.

2) Project License, which authorizes the export of commodities required for a specified activity for a period of approximately one year from the issuance of the license. A renewal licenses may be issued.

3) Distribution License, which authorizes the export of certain commodities to approved cosignees in country groups T and V during a period of one year. It can be renewed The cosignees must be foreign distributors or users of the licensed commodities.

4) Qualified General License, which authorizes the multiple export of certain commodities to an approved cosignee in Country groups Q, W, and Y for a period of one year. The validity period can be extended once for an additional two years. The prospective cosignee must be the actual or prospective user of the licensed commodity.

5) Service Supply (SL) License, which authorizes a U.S. Exporter or Manufacturer to export spare and replacement parts to country groups T, V, (with more restrictions on Q, W, and Y) to service equipment exported by the licensee or

made by his foreign subsidary.

General Licenses are presented under Parts 371 and 379 in the manual. There are 17 general licenses discussed in Part 371 and two that deal with technical data under Part 379. All licenses in this category are designated with a 'G'. Because these are general licenses no applications are required and no license documents are issued. If the technical data does not qualify under the two general licenses covered under Part 379 then a Validated license is required.

The general licenses related to technical data are:

1) GTDA covers technical data generally available to the public and certain foreign origin data. It covers all destinations.

2) GTDR deals with technical data not exportable under the GTDA but exportable subject to specified restrictions. It generally deals with products exported to country groups T and V. Under special circumstances exports to country groups Q, W and Y are permitted.

Some of the products under the non technical general licenses of Part 371 may seem too obvious and are as followed;

1) G-DEST covers the shipment of all commodities whose Commodity Control List classification identifies that a validated license for specific destinations is not required.

2) GIT deals with all intransit shipments of commodities except certain defined categories whose destinations are in the country groups of Q, T, V and Cuba.

3) GLV covers shipments of products in limited value country groups of T, O, and V.

4) G-FTZ deals with the export of petroleum products from U.S. Foreign Trade Zones and Guam to all destinations.

5) G-COM covers those commodities whose technical performance characteristics are specified in the Advisory Note. The destinations are the COCOM countries.

6) RCS deals with all shipments to U.S. or Canadian vessels, planes, airline installations or agents abroad. The country groups covered are Q, S, T V, W, and Cuba.

7) CREW covers the shipments of all usual and reasonable personal effects to all destinations.

8) GTE covers the temporary export of shipments for use abroad and return to the U.S. of specified commodities whose destinations may vary.

9) GUS covers the shipments to members of U.S. Armed Services and Civilian personnel of U.S. Government for personal use and official use in the defined categories. All destinations are covered.

10) GTF-US deals with shipments of commodities for display at exhibitions or trade fairs. These are generally applied to country groups T and V with special circumstances for countries in group W, Q, and Y.

11) G-MNR covers shipments of certain Non-Navel Reserve Petroleum Commodities, for all destinations except countries in groups S and Z.

12) GLR deals with shipments of replacement parts for specified commodities. It covers all destinations except groups S, Z and Iran with some exceptions under certain circumstances.

13) GIFTS covers the shipments of gift parcels from individuals for all destinations of commodities with a ECCN number followed by an A, B, or M.

14) GATS authorizes the departure of civil aircraft either foreign or domestic registration on temporary sojourn to all destinations.

15) SHIP STORES deals with all ship stores used in outgoing voyages to all destinations except those vessels registered or controlled by countries in the control groups Q, W, Y and Z.

16) PLANE STORES is the same as SHIP STORES.

17) BAGGAGE deals with the shipment of personal and household items to all destinations with some exceptions to the country groups T and V identified in the letter following the Export Control Commodity Number.

Once the type of license needed has been identified it needs to be applied for as specified in Parts 371, 372 and 379 of the manual

LICENSING PROCEDURES

FIGURE 4 identifies the time periods involved in the process. It has been streamlined to 180 days from the original 240. The initial screening of a license now only takes 10 days. Major delays can occur in the process when another agency is involved or COCOM action is required. The most important thing to remember is to make sure the application form is completely and properly filled out. A sample of a completed form is included as an exhibit in the appendix.

SUMMARY

One point which was not brought up earlier in the discussion on enforcement was the Export Administration's publication of the Export License Denial Orders. The is a published list of companies who have been denied the privilege of exporting. The list is updated periodically by the Office of Export Enforcement (OEE). Having a current copy of this list is important because you may have your own export license revoked or denied if you are found to be dealing with a company on the list. As the user of an export license it is your responsibility to determine the honesty of your customer. FIGURE 5 provides a one page example of the "DENIAL ORDERS" list.

As mentioned earlier there are several sample forms included as exhibits in the Appendix. The first exhibit identifies the names and numbers of the different forms used in the Export Licensing program. Some of the forms exhibited have instructions included. They are presented in the order indicated on Exhibit 1.

FIGURE 1

Secretary Of Commerce | | Under Secretary For International Trade | | Assistant Secretary For Trade Administration | | Deputy Asst Secretary Deputy Asst Secretary Deputy Asst Secretary For Import---------------For Export Administration------For Export Enforcement Administration | | DIRECTOR OFFICE OF EXPORT ADMINISTRATION | | Technical Program Staff-----------Operating Committee | -- | | | Capital Goods & Production | Computer Services Division | --- | | | | | Foreign Availability Exporter Policy Planning Operations Scientific & Electronic Division Assistance Division Division Equipment Division | Division | | | | | | | | Technical Data Exporter East-West Free World Electronic Components Collection Counseling Trade Licensing and Instrumentation | | | | | Comparative Publications and Strategic Multiple Computer Systems Capabilities Regulations Rating Licensing | | | | | Information Special Processing Microcomputers and Analysis Programs | Telecommunications | Distribution

FIGURE 2

Can shipment be made under general license authorization, e.g., G-DEST, GLV, etc? (Check Parts 399, 371 and 379) | --- \|/ \|/ Yes No | | \|/ \|/ Place Destination Control Statement Prepare application for license (see on commercial documents, if required Part 372 and instructions on reverse (386.6) of application form. ITA-622P) | | \|/ \|/ Is Shipper's Export Declaration Is supporting documentation required? required? (386.3) (Check Parts 375 and 376) | | | | \|/ \|/ \|/ \|/ No Yes Yes No | | | | | | \|/ \|/ | | Obtain documentation and File application | | attach to application with OEA | | | | | | \|/ | | | File application and required | | | documentation with OEA | | | | | | \|/ \|/ \|/ | Submit Shipper's Upon receipt of license (Form ITA-628). | Export Declaration prepare Shipper's Export Declaration | to carrier (386.3) | (386.3) | | | \|/ | | Place Destination Control Statement on -->Make shipment<-- commercial documents (386.6) | \|/ Submit Shipper's Export Declaration to carrier (386.3) | \|/ Make shipment and complete

Record of Shipments on reverse of license (386.2) | \|/ Return license to OEA

EXPORT CONTROL FLOW CHART--This is intended as a general guideline for exports of commodities under Department of Commerce jurisdiction. However, it is not comprehensive. You should review other parts of the Regulations, for example, for special commodity restrictions and special country restrictions. Also, you should consult the "Table of Denial Orders Currently in Effect" (see Supps. Nos. 1 & 2 to Part 388) to be sure your proposed export does not involve a party currently denied export privileges.

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FIGURE 3

Commodity Central Line--Index (A-C) 399.1--Index-1

ALPHABETICAL INDEX TO THE COMMODITY CONTROL LIST

Description ECCN (1) Proc(2) Page Code

 _________________________ (1) ECCN is the Export Control Commodity Number for a particular Commodity Control List entry and Proc. Code is the Processing Code for that particular entry.

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FIGURE 4

Initial Screening 1 if Incomplete or incorrect, return Additional OEA Review Required without action (RWA) to applicant ------> Applicant notified by acknowledgement form 2 Approve or deny in licensing | 10 days and return to applicant | \|/ Application and case YES Referral to NO analysis forwarded <------ other agencies----- to other agencies | | | | | 20 days | | ----------------------- | \|/ \|/ | Request for additional Recommendations of | 2.0 days made by other agencies | other agencies submitted to OEA | | | | 40 days \|/ | \|/ Recommendations of | Cases not referred to other agencies | other agencies are submitted to OEA | approved or denied | | | | 60 days \|/<-------------------- Negative YES Notify Consideration------------------------>Applicant | | NO \|/ --------- Approve<-----COCOM<-------- \|/ | YES | Applicant YES YES \|/ | Rebuttal-------->Reconsider----- Notify applicant | NO | | NO | of referral | -------------------- | | |

\|/ | | | Deny | | -- 120 days | Note: If other agencies do not request additional \|/ 0 days, these steps are to be completed in 150 days COCOM YES action-------Approve | or deny | 180 days \|/ Notify Congress and applicant every 60 days

MAKING MONEY VERSUS MAKING PROFITS: UNDERSTANDING FUNDS FLOWS

by Herbert L. Lyken University of Massachusetts at Boston

A Business Opportunity

Three months before Mr. Jones actually took over ownership of the XYZ Company, he had been presented with the offer to acquire the going business at a very attractive price. After careful analysis of the industry and the business in general, Mr. Jones reached a conclusion that this was a wonderful opportunity. In early January, he went through with this purchase.

Developing the Opportunity

With a reasonable cost and some concerted effort, Mr. Jones was able (through the addition of some new equipment) to make certain improvements to the product-line of his newly acquired business. The improvements were accomplished in a manner that would improve service to his customers, in terms of faster delivery, and more liberal terms of credit than those available in the past. All these moves resulted in greater acceptance of his products by the customers. He felt confident that, with the new practices in place, the sales and profits should increase substantially over those of the previous year. He sincerely believed that if the business was to be successful and to grow, he must operate it efficiently, to be conscious of costs all the time, develop and maintain good working relationships with his customers and suppliers. He exercised great care in the purchase of materials and supplies, and did not allow any of his inventories to exceed the amount of total shipments of the immediate preceding quarter. He paid bills from his suppliers promptly and was able to take advantage of each and every available cash discount.

During the first year, the sales volume grew steadily month after month. He rigorously stuck to his policy of controlling inventories and the day-to-day expenses. At the end of the operating year, Mr. Jones asked his accountant to prepare the financial statements and income tax returns for the company. The accountant determined that the company had made a tidy profit, and that there would be a reasonable amount of income tax obligation. In his efforts to keep the profit and income tax liability to a legal minimum, the accountant valued the inventories on the Last-In, First-Out basis and used an accelerated method of depreciation in relation to the plant and equipment. Knowing fully well that his company had been quite successful during its first year, Mr. Jones happily filed away each of the financial statements. (See Exhibits I, II, and III.)

EXHIBIT I THE XYZ COMPANY Income Statement for the Year Ended December 31, 19xx

Gross Sales $407,000

Less: Returns and allowances $ 3,000 Discounts allowed 8,000 11,000 ----------- ----------- Net Sales 396,000

Less Cost of goods sold:

Finished goods, Jan. 1 14,300

Raw materials, Jan. 1 55,000 Purchases 137,000 ------------ Total 192,000 Less Raw materials, Dec. 31 61,000 ------------ 131,000

Goods in process, Jan. 1 24,200 Additions 129,000 ------------ Total 153,800 Less goods in process, Dec. 31 24,800 129,000 ------------

Supplies, January 1 16,500 Purchase 13,000 ------------ Total 29,500 Less finished goods, Dec. 31 14,500 15,000 ------------ ----------- Total cost of goods manufactured 289,000 Less finished goods, Dec. 31 16,300 ----------- Cost of goods sold 273,000 ------------- Gross margin 123,000 Less other expenses: Selling & administrative 67,000 Depreciation 13,400 Interest 1,875 82,275 ------------ ----------- Income before income taxes 40,725 Less income taxes 15,700 ----------- Nets income $25,025 ------------

EXHIBIT II THE XYZ COMPANY Comparative Balance Sheet

December 31 Current Previous ASSETS Year Year Current Assets

Cash $13,700 $25,500 Accounts receivable 52,200 60,500 Inventories: Finished goods 16,000 14,300 Goods in process 24,800 24,200 Raw Materials 61,000 55,000 Supplies 4,500 16,500 ------------ ------------- Total Current Assets $182,500 $196,000 Prepaid Expenses 6,700 5,700 Property, plant, and equipment 335,000 320,000 Less allowance for depreciation (113,400) (100,000) ------------ ------------- 221,600 220,000 ------------ ------------- Total Assets $410,800 $421,700

LIABILITIES AND OWNERSHIP Current Liabilities

Accounts payable and accruals $ 10,875 $ 20,000 Unpaid taxes 15,000 3,500 ---------- ------------ Total Current Liabilities 26,575 23,500 Notes payable 15,000 33,000 ------------ ------------ Total Liabilities 41,575 56,500

Ownership

Balance, Jan. 1 $365,200 Less dividends paid (21,000) ------------ 344,200 Add net income for one year 25,025 ------------ Balance of ownership, Dec. 31 369,225 365,300 ----------- ------------ Total Liabilities and Ownership $410,800 $421,700 ----------- ------------

EXHIBIT III THE XYZ COMPANY Statement of Changes in Financial Position For the Year Ended December 31, 19xx

Working capital provided from: Net Income $25,025 Add charges against earnings not affecting working capital: Depreciation 13,400 ---------- Working capital provided from operations (Also total working capital provided) 38,625

Working capital used for: Acquisition of property, plant, and equipment 15,000 Increase in prepaid items 1,000 Reduction of notes payable 18,000 Dividends paid 21,000 ----------- Decrease in working capital $16,575 -----------

Increase (decrease) in working capital consisted of: Decrease in cash $(11,800) Decrease in accounts receivable (8,300) Increase in Inventories 6,600 Decrease in accounts payable and accruals 9,125 Increase in liability for unpaid taxes (12,200) ----------- Decrease in working capital $(16,575)

A Surprise

Thereafter, the first income tax payment to the Internal Revenue Service became due. Mr. Jones was dismayed to learn that the company did not have enough cash on hand to meet the legal obligation. Hence Mr. Jones decided to approach his bank for borrowing money to take care of income tax payments. He was greatly upset and wondered where things went wrong. How is it possible that the company made a profit and yet lost money?

In spite of being cost conscious and profit oriented, Mr. Jones failed to recognize that if his firm was to stay in business, to enjoy financial stability, and to grow, it must not only make a profit each year, but even more importantly, it must manage its cashflows in such a way so as to assure continuous solvency. To accomplish this, every business manager needs to be constantly aware of his financial management responsibilities. That means he must constantly keep track of cash or credit (which at times can temporarily take the place of cash) flowing into the business. The inflows should always be sufficient at least to meet the amount of funds flowing out of the business. Managing the flow of funds may look relatively simple, but it is vitally important to the existence and welfare of any business, whether large or small.

Profit Determination Based on Judgements

It is crucial that people in business understand the difference between the profits and the flow of funds. In its simplest terms profit represents the difference between the revenues (usually derived almost entirely from sales) and the costs (cost of goods sold as well as other period costs, including depreciation and amortization.) Profits, as measured by the accountants, recognize the matching of expenses with revenues for each accounting period during which the associated goods and services were delivered (i.e. the proceeds) or consumed (i.e. the costs.) Such proceeds and costs are not necessarily represented by cash inflows or outflows, but rather result from the consistent application of acceptable or relevant and conservative accounting principles. Accountants promote professional expressions of opinion as to the relevancy and conservatism in the application which they apply in the determination of revenues and costs that are reported to the owners of the business, taxing authorities, or to any other interested parties. Profits, therefore, are based on estimates, judgements, and opinions of accountants about the revenues and expenses, and not on the dynamics of cash or credit.

While in most cases proceeds from the sale and delivery of goods and/or services result in revenues for the accounting period in which the delivery is made, still the professional determinations must be made to assure that revenues relating only to the accounting period under consideration are reported. Estimates and judgements must also be made about the expenses that have provided benefits to the business for the accounting period under consideration, without any regard to whether the funds were spent during this very period. The most important among such estimates could be the determination of cost of goods sold and the and the calculation of depreciation for capital assets. The cost of goods sold and the inventory valuations are normally computed simultaneously. The important judgements are always about the valuation of inventories on a First-In, First-Out (FIFO) basis, on a Last-In, First-Out (LIFO) basis, or on some other basis. Depreciation is most often based on the educated estimate of the length of productive life of the capital assets in question, and also on the judgement regarding the method of depreciation to be used. Depreciation might be computed on a straight-line basis, which is the most commonly used method when businesses report their earnings to their owners. Further, the depreciation may be calculated using one of the accelerated methods (e.g., double-declining-balance method, sum-of-the-years-digits method, or any acceptable method that provides accelerated depreciations) especially for reporting to tax authorities. Based on the legitimate use of the above types of variety of judgements, it has become quite permissible for firms to report quite a different figure to the Internal Revenue Service than the one reported to its owners and other relevant groups.

Making Money Is Result of Actual Transactions

Receipts and disbursement of funds are made upon the exchange of goods and services between the two parties concerned. These exchanges involve definite dollar amounts as agreed upon by the two parties. This, of course, leaves no room for the exercise of any judgement as to the amounts to be recorded in the books of each side. The meaning of the term "funds" centers around the concept of means of payment, whether in cash or through a promise to pay or receive cash at some later date. The exchange of funds is accompanies by the exchange of goods and/or services (by way of a sale or a purchase) between two independent parties, one of whom has control over the supply of goods and/or services for sale, while the other has control over the supply of funds. Funds flow results from the difference between the cash or a promise to receive cash which is accepted by one entity from some external source with cash or the promise to pay cash which goes out of the second entity during a designated period of time. Each and every transaction involving the exchange of funds for goods and services is called an external exchange and it always results from considerations that are entirely factual.

Looking back to the end-of-year's cash situation of Mr. Jones can readily show that his success in making a profit did nothing to assure his success in developing the financial stability so necessary for the maintenance and growth of his company. Mr. Jones seems to have failed in making good decisions about the management of credits, both as to the granting of credit to his customers and to the negotiating of credit which is often possible from suppliers. In establishing credit policies, it would have been wise for Mr. Jones to have kept a reasonable balance between extending the credit and obtaining credit, such that the cash might have flowed in faster than it flowed out as settlements were made. If cash from the settlement of receivables flow is at a much slower rate than it flows out in the settlement of obligations, then the cash shortages become inevitable, making it necessary or the company to tap outside sources of capital. Continued growth of sales would certainly cause a steady deterioration of cash balances. Unless such a condition is quickly rectified, financial disaster becomes a reality, irrespective of the profitability of the business. Therefore, it is extremely important that Mr. Jones as a Company Manager takes steps to improve the company's cash balances by speeding up the collection of his receivables, negotiating easier terms from suppliers and by cutting down the growth of his sales to avoid insolvency.

Analyzing Financial Reports

Mr. Jones, being a non-accountant, tried to analyze the financial reports provided to him by his accountant. He hoped to locate the cause(s) of his cash problems and to determine how he could lead the company through its second year of operations.

Examining the income statement (Exhibit I) he first calculated certain ratios that were important. These calculations indicated that gross margin on his net sales was 31.1% of the net sales and net- after-tax-income amounted to 6.3% of net sales. Comparing these percentages to those of the previous year, and making comparisons with the industry averages, he concluded that these were quite satisfactory. By adding the year's depreciation back to the net earnings, he found his cashflow to be equal to $38,425. Depreciation did not represent any use of cash, therefore, this amount of $38,425 must have been generated by the company operations during the year. He was unable to accept and reconcile this amount of "cashflow" with the year's end cash balance of $13,700 . Only now he realized that cashflow did not really mean cash, and he wondered about the significance of this figure. He was still having trouble explaining to himself how the business could make a profit and still it could lose money.

Next, he went over his comparative balance sheet (Exhibit II) and once again he calculated a few other important ratios. His current ratio (current assets/current liabilities) came out to be nearly 7 to 1, which is extremely high. After deducting the inventories from the current assets, he got a quick ratio of 2.5. Again, he could see that while the overall financial condition of the company appeared to be strong, its cash position was embarrassingly weak. He did, however, determine that the inventories were extremely high and the rate of inventory turnover was quite low. He felt confident that the inventories of raw materials and supplies could be reduced by as much as one- third during the upcoming year without impairing either the rate of or the growth of sales. His decision to reduce inventories would certainly provide needed cash. He wondered why he had waited until after the end of the accounting period to make this simple discovery.

After going over the statement of changes in financial position (Exhibit III), Mr. Jones found it almost impossible to put the figures contained therein into right perspective. He noted that the "cashflow" figure of $38,425 that was given in the income statement did agree with "Working capital provided by operations", but he was still having trouble in understanding just what did it mean. Apart from his observation about inventories, he failed to see how the three financial reports could be of any help to him in day-to-day decision making. Once again, he filed away these reports and started thinking about what to do next.

Funds Flow Accounting*

Professor Hunt has developed a method for analyzing cashflows of a business in a coherent, understandable fashion which should prove to be invaluable to operating managers and investment analysts in assessing the financial strength of any ongoing enterprise. It is a systematic approach to provide a business manager with a set of "hard" numbers about certain business figures (dollar amounts) which can be accepted as facts, untainted by the vagaries of accounting interpretations. This method focuses upon the funds provided by the operations of a business and on funds coming through the financial transactions such as sale of equity or loans. Jointly these flows represent the "funds position" which is invariably a realistic reflection of business's financial strength.

___________________________ * A Working Paper, Harvard School of Business, Boston, Massachusetts 1975.

The Statement of Sources and Applications of Funds for Jones' company for the Year Ended December 31, 19XX (Exhibit IV), has been prepared using Hunt's method. This statement clearly shows that sales were the sole source of operating funds, and these were the funds which took care of the Cost of Goods Sold, Other Operating Costs, and of Income Taxes as well. The leftover amount of $38,425 constituted the "Funds Provided by Operations". Undoubtedly, a business can have a variety of reasons to spend the funds on items such as purchase of inventories or capital investments in property, plant, or equipment. While such acquisitions are generally expensed over a number of accounting periods through standard depreciation and amortization methods, still the payments for all such items must be made immediately and in full amount. Therefore, after deducting $22,600 of funds spent on capital facilities or on deferred cost items, we can obtain the figure of $15,825 which is nothing else but the "FUNDS POSITION". This "Funds Position" is believed to be the keystone of financial planning because it happens to be the best indicator of a company's financial state. Unlike the earnings and cashflow figures, the "Funds Position" not only recognizes a company's operating funds flow, but also reflects the company's need to invest funds for the maintenance of its activities. If the "Funds Position" is a positive number, that means the funds were provided by the business in question to meet the financial obligations that had been entered into by the management. If it is a negative number, that means the amount has come from outside sources (lenders of investors) to fill the financial gaps.

EXHIBIT IV XYZ COMPANY Statement of Sources and Applications of Funds For the Year Ended December 31, 19xx

OPERATIONS Sources of Funds:

Gross sales $407,000 Applications of Funds:

Sales returns and allowances $(3,000) Discounts allowed (8,000) Cost of goods sold (273,000) Selling and administrative expenses (67,000) Interest expense (1,875) (352,875) ----------- ----------- Funds provided by operations, before taxes 56,125 Income taxes (15,700) ----------- Funds provided by operations, after taxes 38,625

INVESTMENTS and other deferred costs

Inventories (6,600) Property, plant & equipment (15,000) Prepaid items (1,000) (22,600) ------------ ----------- FUNDS POSITION 15,825 ----------- FINANCING

Application of Funds:

Decrease in notes payable (18,000) Decrease in accounts payable & accruals (9,125) Decrease in ownership-dividends paid (21,000) (48,125) ------------

Sources of Funds:

Increase in liability for unpaid taxes 12,200 Decrease in accounts receivable 8,300 Decrease in cash 11,800 32,300 ----------- ----------- NET EFFECT OF FINANCING $(15,325)

In this case of XYZ Company, (Jones' company) the "Funds Position" at the end of the year under consideration was a positive number, indicating that the operations of the business were successful enough to result in expansion of funds, as well as in providing for the capital investment and other needs of the business. It must be remembered that "Funds Position" is NOT cash, it is made up partly of cash and partly of promises to receive or pay cash at a later date when settlements of credit (receivables or payables) are made. "Funds Position" is nothing but cash as soon as credits get settled.

In the Financing section of the "Statement of Sources and Applications of Funds", (Exhibit IV), are included-all of the items that concern changes in lending, borrowing or cash. Thus, the net effect of financing (i.e. of the bottom line) is that it offsets the "Funds Position." Sources of funds may include borrowings from suppliers or lenders, disbursing cash, increasing ownership (by way of additional investments and earnings), and collecting accounts due from customers. Applications of Funds can readily be prepared directly from the business ledger accounts and even before financial operating statements have been developed. This statement can be prepared at short intervals during any accounting period and it can serve as an excellent tool in assisting the business manager to follow closely the "Funds Position" of the transactions made with outside parties.

Use of Funds Flow In Forecast And Planning

As perpetuation and growth are generally considered to be the main objectives of business, therefore, the management needs to analyze past financial reports for identifying problems of the past and for evaluating the company's performance. Planning the future is even more important. Like the captain of a ship, the business manager must constantly look ahead, towards the horizon, and establish a definite route and destination to follow. Forecasts and plans need to be made for each of the functional areas -- marketing, personnel, operations, and facilities, and each of these should be coordinated with and worked into an overall financial forecast and aggregate plan. General forecasts and plans are often made for the several years into the future together with detailed plans and budgets covering a relatively shorter interval of a year. The purpose of such plans is to allow enough time for the management, such that they can fully develop their funds requirements, lay down the best course of action to follow, and be ready with the best possible financial support for the projected levels of business activity. Good planning, of course, must always plan for contingencies that may arise beyond every possible precaution taken by the management.

Let us assume that the Jones' Company plans on a five year basis. The format of the "Statement of Sources and Applications of Funds" can be useful even for the five year period of planning and projections. Revenues determined from such sales forecasts would then constitute the major sources of funds. The projections of operating costs, other expenses and of income tax exposures requiring the use of funds could be listed as "Applications of Funds". The difference between the "Projected Revenues" and "Applications of Funds" would be the "Funds Provided by the Operations." "Funds Provided by the Operations" must then be reduced by the dollar amount of projected acquisition of long-lasting productive assets. These assets require the expenditure of funds immediately at the time of their acquisition, regardless of how the accountants might chose to amortize their expense over the years. Further, deducting once more the projected "Applications of Funds" going into deferred cost types of assets, the analyst can obtain the FUNDS PROFILE of the company. The "Funds Profile" integrates all of the plans about the funds requirements over the planning period under consideration.

If the "Funds Profile" figure for any year in question is positive, then the manager can safely conclude that there will be no need for additional outside financing to support the activities during period in question. There could even be a possibility for reducing debt or raising dividend payments to stockholders. If the "Funds Profile" figure for a particular year was negative, then the manager needs to determine immediately whether the company is going broke or it is a reflection of major additions to capital assets for improving the company's productivity and growth potential. A growing business would often have negative "Funds Profile" which means there is an urgent need for outside financing.

The financial planner must consider "Funds Profile" for each planning year as his guiding light to all the other financial arrangements to be made during the following year. Using "Funds Profile" as a tool, the financial manager can provide the required financial resources at all the appropriate times, in proper amounts and at reasonable cost to meet the planned goals and objectives of his company.

Conclusion

It is all too common for business managers and financial analysts to look at the earnings and cashflows of the company as indicators of the financial health of their respective businesses. Profit and cashflow figures tell only a part of the financial story. The amount of profit is not a precise and exact number, it incorporates estimates, judgements and opinions as to how revenues and expenses are determined, and as such, it can be easily and legally manipulated. The term "cashflows" is a misnomer because it relates only to the potential of cash being generated by the operations. No consideration is given to the cash that will be needed to settle the claims and obligations toward acquisition of long-term productive assets and their operating expenses.

"Funds Positions" or "Funds Profile" is a straightforward number that can be calculated from the factual external operating and financial transactions between the company in question and its suppliers and customers. However, it is a number that is rarely, if ever, found on company financial reports. There is an urgent need for a financial statement that will indicate the financial activities of a firm, (as opposed to the financial condition provided by the standard Balance Sheet), and will also report on the factual aspects of the company's transactions with outside parties. "The Statement of Sources and Applications of Funds" (Exhibit IV) can certainly fill the existing gap in a reasonable and satisfying way.

Relying on profits and cashflows as the only indicators of financial health of a company has led many companies, large and small, to financial disaster - because there is a great difference between "Making A Profit and Making Money."

SPREADSHEET MODELS FOR ASSESSING THE VALUE OF A SMALL BUSINESS

Ronald S. Rubin, University of Central Florida

From an economic point of view, a business represents an investment opportunity in which one decides to invest a certain amount of money to start an enterprise. As an investment opportunity, the business could be either more or less valuable than some alternative use of the same money. It is true that such a cold cash concept disregards any personal reasons for entering such a venture; however, personal feelings can, at times, override sound business judgment. Therefore, an unbiased financial valuation should be conducted periodically to determine how valuable an individuals equity position is in the business. Depending upon the outcome of such an analysis, one may want to consider alternative uses for the money.

In addition to an owner's examination of the value of the business, there are others who are interested in the current value of the business. First, when a business is to be sold the owner needs to set a fair price for the firm. How does one arrive at such a fair offering price? Or, if one were interested in purchasing a business, the buyer needs a method in which to evaluate the fairness of the asking price. Second, a business valuation is commonly carried out when a company is trying to attract new equity capital from potential investors. The investors will be interested in the earning power of the firm, long-term profitability, and its capital structure. And finally, it would be wise to examine the value of the business when the company's owner is contemplating taking out key man insurance to protect his personal equity in the business for the benefit of his heirs. So, a business valuation can mean different things to different people, and the significance of the valuation can also vary depending on why the valuation was undertaken. Too low an evaluation can possibly cause a financial hardship if one wanted to attract a potential buyer for the business. Or, if one were seeking to expand through the sale of partial ownership, a low valuation would not bring into the business an appropriate amount of capital to handle the necessary expansion. On the other hand, too high an evaluation could possibly be considered fraudulent. One should try and avoid both of these extremes. However, if one could approximate the lower and upper value boundaries for the business, one will have a realistic understanding of the worth of the business that is owned or are contemplating buying.

No one has a surefire way of valuating the absolute worth of a business. However, it is important to provide a realistic approach in establishing the business' value that is based on the current earning power and on the potential profitability of the business. Such information is fairly easily developed from the three valuation methods offered in this article. One method of evaluation is based on what one knows happened in the past and is termed Capitalization of Past Earnings. The second method is based on what is expected to happen in the years ahead and is known as Discounting of Future Earnings. Both methods rely on an asset valuation as part of the profitability equation; and the other ingredient of that equation is the approximation of either the past or future stream of profits. The third method is a formula, from the Bank of America's Small Business Reporter Series, for arriving at a price for the business. The approach is so uncomplicated and straight forward that it warrants the attention of anyone who is trying to establish a price for an on going business.

SELLING PRICE FORMULA

The following describes the seven steps in the formula and illustrates through a spreadsheet model how they can be applied.

STEP 1. Determine the adjusted tangible net worth of the business by identifying the market value of all the assets and then subtract the debts or liabilities of the business. In Table 1, for a hypothetical company, this has been determined to be $75,000.

STEP 2. Estimate how much the buyer could earn on an annual basis with the amount of money derived from step 1 if it were invested elsewhere. A reasonable figure would depend on the stability and the relative risks of the business and the general investment picture. The rate selected should be similar to that which could be earned elsewhere with the same approximate risk. In Table 1 the earning power has been set at 10 percent. However, if you perceive the considered business to be a very high risk, this percentage should be set higher to reflect the necessary amount needed to be earned at a higher risk venture.

STEP 3. To the figure derived in step 2, add a salary for the owner-operator. The sum of step 2 and step 3 represents a reasonable estimate of the income the buyer can earn if the investment were places elsewhere and the efforts involved in working in the business are taken into consideration. In Table 1 the salary figure has been set at 15,000.

STEP 4. Determine the average annual net earnings (net profit before subtracting owner's salary) before taxes that can be obtained from the business over the past few years. The trend of earnings is a key factor. Have they been rising steadily, falling steadily, remaining constant, or fluctuating widely? The earnings figure should be adjusted to reflect these trends. In Table 1 this figure has been determined to be $27,000.

STEP 5. Subtract the earning power and the salary figure (Steps 2 and 3) from the average net earnings figure in Step 4. This represents the extra earning power that a buyer will obtain by owning the business.

STEP 6. Using this extra earning power figure from Step 5, you now estimate the value of the intangibles. This is done by multiplying the extra earnings figure by an estimate of the number of years for which these extra earnings can be expected to continue. This new figure, in effect, represents the intangible know as "goodwill". If the business is well established and has a valuable name, patent, or location, a years factor of five or more might be used. If the business is a moderately seasoned firm, a multiplier of three might be reasonable. A younger, but profitable, firm might have a one-year profit figure. Obviously, the more well established the business, the greater the amount for goodwill a buyer should be willing to pay and this will be reflected in the appropriate multiplier applied at this stage of the analysis.

STEP 7. The final price is found by adding the figures from Step 1 and Step 6. It is equal to the net market value of the assets plus the value of the intangibles. In this case a value of the business has been set at $90,000 as fair and reasonable.

TABLE 1 SPREADSHEET MODEL FOR DETERMINING THE VALUE OF THE BUSINESS

ASSESSING THE VALUE OF A BUSINESS FILE NAME: BUSVALUE

************************** SELLING PRICE FORMULA **************************

--------------------------------------- DATA INPUT TABLE ---------------------------------------

1. ADJUSTED VALUE OF TANGIBLE NET WORTH: $75,000

2. ALTERNATIVE EARNING POWER: $ 7,500

3. SALARY FOR OWNER/MANAGER $15,000

4. NET PROFIT BEFORE SUBTRACTING OWNER'S SALARY: $27,000

--------------------------------------- DATA OUTPUT TABLE ---------------------------------------

1. EXTRA EARNINGS POWER OF THE BUSINESS: $ 4,500

2. ENTER NUMBER OF YEARS FOR WHICH THESE EXTRA EARNINGS CAN BE EXPECTED TO CONTINUE 3

3. VALUE OF INTANGIBLES: $13,500

4. FINAL VALUE: $88,500

CAPITALIZATION OF PAST EARNINGS

This valuation procedure is best described as a two step process: first calculate the rate of profitability; then develop an "adjusted" rate if need be and use the latter figure in a "capitalization" calculation formula. Let us take a closer look at the procedure.

The rate of profitability (Return on Investment - ROI) can be obtained by using the formula:

ROI = annual profit (or 4 or 5 year's average profit) -- owner's equity

Depending upon the situation, either the most recent year's profit or an average of the last four or five year's profits may be used in the numerator of the fraction. The latter profit figure is preferable unless there has been an unusual earnings pattern making it unrealistic to include the earlier year's profits. Also, it would be more realistic if the owner's equity on the latest balance sheet is entered in the denominator.

The next step is to apply the ROI that was just calculated in a "capitalization" formula or you may want to adjust this figure to reflect the stability of the company and the risks involved investing in such a venture. If the risks seem to be high, you might want to adjust the rate upward to reflect the extra profit needed to make up for the higher risks involved with this venture.

In order to help you comprehend the calculations with this valuation procedure, a simplified illustration is presented. Table 2 highlights the essential income and equity data derived from financial statements, and the outcome of the data inputs.

TABLE 2 SPREADSHEET MODEL USING THE CAPITALIZATION OF PAST EARNINGS TO VALUATION

*************************************** CAPITALIZATION OF PAST EARNINGS ***************************************

------------------------------------ DATA INPUT TABLE ------------------------------------

ENTER ANNUAL PROFIT FOR EACH OF THE FOLLOWING YEARS:

1979 $ 36,400 1980 $ 29,010 1981 $ 33,750 1982 $ 40,600 1983 $ 43,150

ENTER OWNER'S EQUITY FOR THE LATEST YEAR: $ 113,295

------------------------------------ DATA OUTPUT TABLE ------------------------------------

AVERAGE EARNINGS FOR THE LAST 5 YEARS: $ 36,582

RETURN ON INVESTMENT .323

IF WE CAPITALIZE ROI ON AVERAGE INCOME 1979 THROUGH 1983: $ 133,295

IF WE CAPITALIZE ROI ON 1983 INCOME: $ 133,636

The 32 percent rate of return derived is very satisfactory; however, if an investor perceives the business investment to be uncomfortably risky, he may want to raise the rate to, say 35% to take into consideration the additional risk he would be taking if he purchased the venture. Note that if we keep the ROI at the calculated rate and capitalize it on past earnings, we obtain $113,295 if we capitalize it on the average income, 1979 through 1983; or $133,636 if we capitalize it on 1983 income.

This produces a small increase in the value in recognition of the higher earnings in the later year.

DISCOUNTING OF FUTURE EARNINGS

The previous method was based on past values. A capitalization of recent earnings plus a projection of the earnings potential for the future are also considered to be useful in the valuation of a business. The calculations for this method are as follows:

Increase per year

= 1983 income - 1979 income -------------------------------- number of years

= $43,150 - $36,400 --------------------- 5

= $6,750 --------- = $1,350 5

Past income growth based on 1983 income

= $1,350 --------- = 3% per year $45,150

Therefore, assume future income growth will be 3% per year for the next five years.

To find the earnings potential for the future years we can use the data in Table 3, which shows precalculated present values. From this Table you can find the present value of $1 received (n) years from today, at various rates. To estimate the time value of estimated income in a given year, first multiply the income for present year by the income growth percentage. Then multiply that amount by the corresponding factor from the Table. You will derive the present value of the future years in question. By adding together all the present values of future income for each of the years in question, you can determine what the entire income stream is anticipated to produce in the future. This figure is the total value that the business is worth right now. The following example illustrates how the discounting of future earnings is calculated. We assume a future earnings discount of 15 percent which is more than the current rate to borrow funds; however, it may well be that high by 1988, the final year of our future projection. The total present value of estimated future income is $157,487.

CONCLUSIONS

If one were contemplating the sale of the business, the valuation developed under the discounting of future earnings could logically be selected as the asking price. On the other hand, if one were considering the purchase of the company, the capitalization of past earnings might be the offering price for the business. Either of these valuations would be realistic depending upon the choice of the method used for a valuation of a business will be up to you. Any of the methods described here will produce a realistic result.

TABLE 3 PRESENT VALUE OF $1 RECEIVED n YEARS HENCE, AT DIFFERENT DISCOUNT RATES

Years Hence 1% 2% 4% 6% 8% 10% 12% 14% 15% 16% 18% 20% 22%

1 0.990 0.980 0.962 0.943 0.926 0.909 0.893 0.877 0.870 0.862 0.847 0.833 0.820 2 0.980 0.961 0.925 0.890 0.857 0.826 0.797 0.769 0.756 0.743 0.718 0.694 0.672 3 0.971 0.942 0.889 0.840 0.794 0.751 0.712 0.675 0.658 0.641 0.609 0.579 0.551 4 0.961 0.924 0.855 0.792 0.735 0.683 0.636 0.592 0.572 0.552 0.516 0.482 0.451 5 0.951 0.906 0.822 0.747 0.681 0.621 0.567 0.519 0.497 0.476 0.437 0.402 0.370

6 0.942 0.888 0.790 0.700 0.630 0.564 0.507 0.456 0.432 0.410 0.370 0.335 0.303 7 0.933 0.871 0.760 0.665 0.583 0.513 0.452 0.400 0.376 0.354 0.314 0.379 0.248 8 0.923 0.853 0.731 0.627 0.540 0.467 0.404 0.351 0.327 0.305 0.266 0.233 0.204 9 0.914 0.837 0.703 0.592 0.500 0.424 0.361 0.308 0.284 0.263 0.225 0.194 0.167 10 0.905 0.820 0.676 0.558 0.463 0.386 0.322 0.270 0.247 0.227 0.191 0.162 0.137

11 0.896 0.804 0.650 0.527 0.429 0.350 0.287 0.237 0.215 0.195 0.162 0.135 0.112 12 0.887 0.788 0.625 0.497 0.397 0.319 0.257 0.208 0.187 0.168 0.137 0.112 0.092 13 0.879 0.773 0.601 0.469 0.368 0.290 0.229 0.182 0.163 0.145 0.116 0.093 0.075 14 0.807 0.758 0.577 0.442 0.340 0.263 0.205 0.160 0.141 0.125 0.099 0.078 0.062 15 0.861 0.743 0.555 0.417 0.315 0.239 0.183 0.140 0.123 0.108 0.084 0.065 0.051

16 0.853 0.728 0.534 0.394 0.292 0.218 0.163 0.123 0.107 0.093 0.071 0.054 0.042 17 0.844 0.714 0.513 0.371 0.270 0.198 0.146 0.108 0.093 0.080 0.060 0.045 0.034 18 0.836 0.700 0.494 0.350 0.250 0.180 0.130 0.095 0.081 0.069 0.051 0.038 0.028 19 0.828 0.686 0.475 0.331 0.232 0.164 0.116 0.083 0.070 0.060 0.043 0.031 0.023 20 0.820 0.673 0.456 0.312 0.215 0.149 0.104 0.073 0.061 0.051 0.037 0.026 0.019

21 0.811 0.660 0.439 0.294 0.199 0.135 0.093 0.064 0.053 0.044 0.031 0.022 0.015 22 0.803 0.647 0.422 0.278 0.184 0.123 0.083 0.056 0.046 0.038 0.026 0.018 0.013 23 0.795 0.634 0.406 0.262 0.170 0.112 0.074 0.049 0.040 0.033 0.022 0.015 0.010 24 0.788 0.622 0.390 0.247 0.158 0.102 0.066 0.043 0.035 0.028 0.019 0.013 0.008 25 0.780 0.610 0.375 0.233 0.146 0.902 0.059 0.038 0.030 0.024 0.016 0.010 0.007

26 0.772 0.589 0.361 0.220 0.135 0.084 0.053 0.033 0.026 0.021 0.014 0.009 0.006 27 0.764 0.586 0.347 0.207 0.125 0.076 0.047 0.029 0.023 0.018 0.011 0.007 0.005 28 0.757 0.574 0.333 0.196 0.116 0.069 0.042 0.026 0.020 0.016 0.010 0.006 0.004 29 0.749 0.563 0.321 0.185 0.107 0.063 0.037 0.022 0.017 0.014 0.008 0.005 0.003 30 0.742 0.552 0.308 0.174 0.099 0.057 0.033 0.020 0.015 0.012 0.007 0.004 0.003

TABLE 3-Continued

Years Hence 24% 25% 26% 28% 30% 35% 40% 45% 50%

1 0.806 0.800 0.794 0.781 0.796 0.741 0.714 0.690 0.667 2 0.650 0.640 0.630 0.610 0.592 0.549 0.510 0.476 0.444 3 0.524 0.512 0.500 0.477 0.455 0.406 0.364 0.328 0.296 4 0.423 0.410 0.397 0.373 0.350 0.301 0.260 0.226 0.198 5 0.341 0.328 0.315 0.291 0.269 0.223 0.186 0.156 0.132

6 0.275 0.262 0.250 0.227 0.207 0.165 0.133 0.108 0.088 7 0.222 0.210 0.198 0.178 0.150 0.122 0.095 0.074 0.059 8 0.179 0.168 0.157 0.138 0.124 0.091 0.068 0.051 0.039 9 0.144 0.134 0.125 0.108 0.094 0.067 0.048 0.035 0.026 10 0.116 0.107 0.099 0.085 0.073 0.050 0.035 0.024 0.017

11 0.094 0.086 0.079 0.066 0.056 0.037 0.025 0.017 0.012 12 0.076 0.069 0.062 0.052 0.043 0.027 0.018 0.012 0.008 13 0.061 0.055 0.050 0.040 0.033 0.020 0.013 0.008 0.005 14 0.049 0.044 0.039 0.032 0.025 0.015 0.009 0.006 0.003 15 0.040 0.035 0.031 0.025 0.020 0.011 0.006 0.004 0.002

16 0.032 0.028 0.025 0.019 0.015 0.008 0.005 0.003 0.002 17 0.026 0.023 0.020 0.015 0.012 0.006 0.003 0.002 0.001 18 0.021 0.018 0.016 0.012 0.009 0.005 0.002 0.001 0.001 19 0.017 0.014 0.012 0.009 0.007 0.003 0.002 0.001 20 0.014 0.012 0.010 0.007 0.005 0.002 0.001 0.001

21 0.011 0.009 0.008 0.006 0.004 0.002 0.001 22 0.009 0.007 0.006 0.004 0.003 0.001 0.001 23 0.007 0.006 0.005 0.003 0.002 0.001 24 0.006 0.005 0.004 0.003 0.002 0.001 25 0.005 0.004 0.003 0.002 0.001 0.001

26 0.004 0.003 0.002 0.002 0.001 27 0.003 0.002 0.002 0.001 0.001 28 0.002 0.002 0.002 0.001 0.001 29 0.002 0.002 0.001 0.001 0.001 30 0.002 0.001 0.001 0.001

TABLE 4 SPREADSHEET MODEL USING THE DISCOUNT OF FUTURE EARNINGS APPROACH TO VALUATION

** DISCOUNTING OF FUTURE EARNINGS **

--------------------------------- DATA INPUT TABLE ---------------------------------

ENTER THE FOLLOWING: LATEST YEAR INCOME: $43,150 EARLIEST YEAR INCOME: $36,400 NUMBER OF YEARS: 5 DISCOUNT FACTOR FOR THE FOLLOWING YEARS:

1984 .87 1985 .756 1986 .658 1987 .572 1988 .497

----------------------------------- DATA OUTPUT TABLE -----------------------------------

PAST INCOME GROWTH BASED ON 1983 INCOME: 3.13%

ESTIMATED INCOME FOR THE FOLLOWING YEARS:

1984 $ 44,500 1985 $ 45,892 1986 $ 47,328 1987 $ 48,809 1988 $ 50,336

PRESENT VALUE OF FUTURE INCOME FOR THE FOLLOWING YEARS:

1984 $ 38,715 1985 $ 34,695 1986 $ 31,142 1987 $ 27,919 1988 $ 25,017

TOTAL PRESENT VALUE OF ESTIMATED FUTURE INCOME IS: $157,487

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A1'ASSESSING THE VALUE OF A BUSINESS A2"FILE NAME:BUSVALUE A3 \ * A4'SELLING PRICE FORMULA A5 \ * A6'DATA INPUT TABLE A7 \ -------------------- A8'1. ADJUSTED VALUE OF A9' TANGIBLE NET WORTH: A10 AII'2. ALTERNATIVE EARN- A12' ING POWER: A13 A14'3. SALARY FOR OWNER/ A15' MANAGER: A16 A17'4. NET PROFIT BEFORE A18' SUBTRACTING OWNER'S A19' SALARY: A22 \ * A23'CAPITALIZATION OF PAST EARNINGS A24 \ * A25'DATA INPUT TABLE A26 \ - A27'ENTER ANNUAL PROFIT A28'FOR EACH OF THE FOLLOW- A29'ING YEARS: A30 1979 A31 1980 A32 1981 A33 1982 A34 1983 A36'ENTER OWNER'S EQUITY A37'FOR THE LATEST YEAR:

A41 \ * A42'DISCOUNTING OF FUTURE EARNINGS A43 \ * A44'DATA INPUT TABLE A45 \ - A46'ENTER THE FOLLOWING: A47' LATEST YEAR INCOME: A48' EARLIEST YEAR INCOME: A49' NUMBER OF YEARS A50' DISCOUNT FACTOR FOR A51' THE FOLLOWING YEARS: A52^1984 A53^1985 A54^1986 A55^1987 A56^1988 B9(CO) 75000 B12(CO) 7500 B15(CO) 15000 B19(CO) 27000 B22 \ * B24 \ * B30(CO) 36400 B31(CO) 29010 B32(CO) 33750 B33(CO) 40600 B34(CO) 43150 B37(CO) 113295 B41 \ *

B43 \ * B47(CO) 43150 B48(CO) 36400 B49 5 B52 .87 B53 .756 B54 .658 B55 .572 B56 .497 C6'DATA OUTPUT TABLE C7 \ ------------- C8^EXTRA EARNINGS POWER C9^OF THE BUSINESS:

Cll' ENTER NUMBER OF YEARS C12' FOR WHICH THESE EXTRA C13' EARNINGS CAN BE EX- C14' PECTED TO CONTINUE:

C16' VALUE OF INTANGIBLES:

C18^FINAL VALUE: C25'DATA OUTPUT TABLE C26 \ - C27'AVERAGE EARNINGS FOR C28'THE LAST 5 YEARS:

C30'RETURN ON INVESTMENT:

C32'IF WE CAPITALIZE ROI C33'ON AVERAGE INCOME C34'1979 THROUGH 1983:

C36'IF WE CAPITALIZE ROI C37'ON 1983 INCOME: C44' DATA OUTPUT TABLE C45 \ - C46'PAST INCOME GROWTH C47"BASED ON 1983 INCOME: C50"ESTIMATED INCOME FOR C51"THE FOLLOWING YEARS: C52^1984 C53^1985 C54^1986 C55^1987 C56^1988

C58^PRESENT VALUE OF C59"FUTURE INCOME FOR THE C60^FOLLOWING YEARS: C61^1984 C62^1985 C63^1986 C64^1987 C65^1988

C67'TOTAL PRESENT VALUE C68'OF ESTIMATED FUTURE C69'INCOME IS: D9(B0) +B19-(B12+B15) D14 3

D16(D1) +D9*Dl4

D18(B0 +B9+D16 D19 \ ========== D28(B0) @SUM(B30)..B34)/(A34-A30+1)

D30(D3) +D28/B37 D34(D0) +D28/D30

D37(B0) +B34/D30 D47(B2) ((B47-B48)/B49)/B47 D52(B0) ((B47*D47)+B47) D53(D0) +D52*D47+D52 D54(D0) +D53*D47+D53 D55(D0) +D54*D47+D54 D56(D0) +D55*D47+D55 D61(D0) +D52*B52 D62(D0) +D53*B53 D63 (D0) +D54*B54 D64(D0) +D55*B55 D65(D0) +D56*B56 D69(D0) @SUM(D61..D65) D70 \ =

THE USE OF ACCOUNTING DATA IN SMALL BUSINESS VALUATION

Lawrence D. Lewis, Gonzaga University

ABSTRACT

The main factors affecting the value of a business are:

1) What it owns. A firm's assets will be detailed on an audited Statement of Financial Position (Balance Sheet). The accounting value of these assets, however, may or may not have a relationship to their market value.

2) What it earns. It is important to determine the composition of key Income Statement accounts. Will past relationships hold in the future?

3) What risks it faces. This is the most difficult of the three main factors to assess. There are, however, several areas to look at closely.

INTRODUCTION

The main factors affecting the value of a business (small or otherwise) are: the age and condition of its assets, its potential future earnings, and the risk it faces. This article will explore these factors and the roles they play in the evaluation of small businesses.

If a prospective buyer does not examine a firm from the perspective of these valuation factors, he is taking the unnecessary chance that what he is buying is not what the seller purports it to be, i.e., a profitable, on-going concern. On the other hand, if a prospective seller does not consider the role these factors play in the valuation of his firm and does not spend a considerable amount of time and energy preparing his business for sale, he may have to sell the business for less than would otherwise be necessary. In addition to the purchase and sale of firm, there are also a number of other situations where the valuation of a firm is desirable. These situations include the retirement of a principal financing arrangements, divorce, estate settlements and tax audits. (1, p. 70)

Before proceeding further, one important point should be stressed; the valuation of a business enterprise is not an exact science. While a sound valuation is based on relevant facts, elements of' common sense and informed judgment also play a central role in the valuation process.

There are two important factors to keep in mind when considering valuation techniques. First, one must use those techniques which are appropriate to the nature of the business. For example, techniques utilizing balance sheet values are more appropriate when appraising companies whose assets are largely liquid and subject to fairly accurate accounting valuation. (2, p. 44) Conversely, such techniques would not be applicable if the business's primary asset is a ten-year old apartment building because the balance sheet value of such an asset has little or no relationship to its current market value. Second, one should not limit the appraisal analysis to one technique. The use of several appropriate techniques will result in range of values within which the buyer and seller can negotiate. The use of several valuation methods will help raise negotiations above personal opinion to rational analysis.

THE FACTORS

A set of audited financial statements will help in determining what the firm's assets are and what it earns. These statements and their elements need to be scrutinized closely.

The Firm's Assets

To determine what a company owns, begin with the company's balance sheet. The balance sheet (often referred to as Statement of Financial Position) will list the assets the company owns, but generally will show only their historical cost or some other accounting value. To determine a usable value of the firm's assets these balance sheet values will have to be adjusted. Add appreciation, where appropriate, for increases in the value of assets such as real estate, inventory, equipment and marketable securities. The book value of these assets seldom reflect their current market value. Include a value for intangible assets such as goodwill if they are present. Devalue any questionable assets such as outdated inventory or old receivables. Also, look closely at loans to or from the present owner. Investigate the circumstance surrounding such loans. Hidden problems or opportunities can sometimes be revealed by such investigation. Ask why the owner made such loans to the firm.

What the Company Earns

The relevant earning power of a business is what it can earn under your management, which may very well be different than what it earns under the current management. In evaluating a small business, one can get an idea of how well it has been managed and its earning potential by comparing its recent performance with the performance of similar businesses and by comparing its recent performance with its performance of earlier periods.

In evaluating a firm's earning potential the best place to start is the firm's audited income statement. The revenue and expense accounts should be closely scrutinized. It is important to understand the relationship between key amounts such as net income and sales in order to determine the profitability of the firm. It is equally important to determine the composition of key accounts. The true earning potential of closely held companies can be obscured by a number of techniques used to obscure inefficiencies, reduce taxes, or favor the owners.

The following is a list of several accounts that warrant particularly close attention.

Inventory. To determine whether merchandise inventory was purchased at reasonable prices, compare the invoices of recent purchases with market prices. You may uncover an opportunity to reduce the cost of goods sold, or you may find that inventory which the owner bought at bargain prices is no longer available.

Wages. This is an area of potential savings or problems. Does the firm indeed need the services of all its employees, or are needed services (such as maintenance) going unrendered in an attempt by the present owner to bolster short-term profits? Is the current wage structure adequate and fair, or are the employees due a substantial raise?

Administrative expenses. One purpose of closely analyzing the income statement is to uncover inefficiencies, as they represent hidden earning potential. Administrative expenses generally include accounting, personnel, clerical, and management costs. These areas are often the source of inefficient operations. It often pays to take a close look at the functions personnel in these areas perform and ask the related questions, "Does this function need to be performed?" and "Could this function be performed more efficiently in another manner?"

Repair and maintenance. Is the current amount spent o the repair and amount spent on the repair and maintenance of the firm's equipment adequate to properly maintain it? This is an area where costs can easily be deferred in order to increase short-run profits. Long-term profitability, of course, will suffer if such a policy is pursued for very long.

Owner's compensation. In many small companies the amount reported for owner's compensation does not reflect the true value of the service rendered. Examine the owner's job. In many cases the owner of a small business is a jack-of-all-trades. It may take a couple of people to replace him. Look at the owner's benefits (use of a company car, use of other company assets, expense account, life insurance, etc.). Be especially watchful for very low compensation as this may mask some earnings difficulties.

Risk

Due to differences in the quality and philosophy of different managements, the risk associated with a given firm will vary according to the management of the firm. A firm's risk will be different under your management than it is under the current owner's management. For this reason, of the three factors affecting a firm's values, risk is the most difficult to assess. There are, however, several factors to consider which affect risk, regardless of management.

Debt. The amount of debt in relationship to the amount of total adjusted assets is the single most important determinant of risk. Very simply, the higher the percentage of debt, the lower the protection for both creditors and the owner should the firm's fortunes reverse.

Age. Most business failures occur within the first few years of a firm's existence. An older, more established firm should, therefore, be a less risky investment than one only a year or two old. (3)

Customers. A firm that relies on a few large customers for the bulk of its business poses a higher risk than one with a broader customer base. The loss of a large customer has proven fatal to more than one small business.

Personnel. A firm that relies heavily on the knowledge and skill of a few key personnel is in a riskier position than a firm where personnel are widely trained and capable of performing a number of tasks. This risk can sometimes be mitigated, however, through a key-man insurance policy and through the cross-training of employees.

Cost of goods sold. A high risk situation often exists if the cost of goods sold constitutes a large percentage of sales. This situation poses a high risk because the costs of goods sold as usually hard to control. If these costs are too high in relation to sales, gross profit may be inadequate to cover administrative and marketing costs and still provide an adequate return to the owner.

Risk/Reward Tradeoff. In one respect, at least, an investment in a small business is like any other investment, i.e., there should be a reasonable risk/reward tradeoff. The higher the perceived risk, the higher the potential return should be. The total return from an investment in a small business should provide an adequate salary to compensate the owner for the value of his services and provide an adequate profit to compensate for the level of risk assumed.

CONCLUSION

In the final analysis, the value of a firm is somewhat subjective. If a firm changes hands, the final price will be arrived at through negotiations. The use of a valuation framework can, however, enhance the negotiation process by establishing a price range and raise the negotiations from the level of personal opinion to rational analysis.

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ADVISORY BOARDS FOR SMALL BUSINESS: WHO USES A BOARD WITH WHAT RESULTS

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ABSTRACT

Advisory boards are resources for expanding managerial resources and increasing the success rate of business owners. Incidences of businesses using advisory boards are now being recorded. What businesses are using advisory boards with what results? This study was designed to determine the composition and use of advisory boards for small businesses. Businesses using advisory boards are identified in two geographic areas. Characteristics of the composition of the boards are noted and recommendations made for increased formation of advisory boards.

INTRODUCTION

The use, composition, and compensation of boards of directors for large companies is a frequent area of study. (10) (8) (2) (13) (12) (6) Small business boards are also studied. (11) (5) There are articles justifying the value to large and small business owners of advisory boards based on a few examples. (3) (4) (7) (9) There is, however, little information about the extent of use of advisory boards by small business owners or consensus on what model might work best for advisory board development. This study was an attempt to determine the extent of use of advisory boards by small business.

Advisory boards are but one form of management assistance that small business owners may utilize. Boards of Directors, Networking groups, Round-table groups, Start-up and Business plan Forums such as the MIT Forum, memberships in business organizations such as the Rotary Club, and Chambers of Commerce may serve similar functions. In the model as used here, an advisory board is usually composed of from one or more people who are not members of the firm. Usually there are three to five members who are non-paid. These members serve to give the owner or chief executive advice. Ideally, the advisors are selected to complement the skills and abilities of the owner. The advisors serve as a sounding board, advisors, information sources, analysts, moral supporters and critics. The advisors are chosen by the owner or chief executive ultimately. The advisors have no legal obligation nor authority. The non-paid aspect of the boards as defined helps clarify the non- existence of liability for professionals such as attorneys, accountants, or management consultants.

METHODOLOGY

The target populations for this study were all businesses in King, Pierce, and Snohomish Counties referred to as Puget Sound or PS and all the small businesses in the San Francisco Bay area referred to as SF. The intent was to find businesses with advisory boards in order to determine how useful a tool an advisory board might be for a small business.

Any attempt to sample randomly in order to glean statistical significance, became meaningless. In both the PS and SF samples, initial attempts at random sampling were made. It was felt by the researchers that more useful information could be developed by consciously trying to find companies, with under 50 employees, who used advisory boards.

Initially, however, in the PS area, two sets of random clusters were selected from a standard local business directory in the PS area. Out of an initial sampling of 213 businesses (out of a possible 40,000), 61 of the business owners could not be reached by phone after at least two attempts. Seventeen would not cooperate. Thirty-three had gone out of business. From the 102 valid responses, only three owners were found to be using advisory boards. Owners had also been asked if they knew of companies who did use advisory boards. Although seven said yes only one as able to furnish enough information to interview another owner. The researchers used the local Small Business Administration for possible referrals as well as a consultant and a local authority on advisory boards. The local authority provided two names--one of which had already been identified. Professors and other consultants were consulted. In the PS area the researchers were able to identify eight companies who had advisory boards which fit the following definition:

Advisory Boards are one or more outside people who can give the small business owner or president advice. They differ from a board of directors in that they serve as advisors only; the owner is not legally obligated to take their advice.

In the SF area, both random sampling and plain old sleuthing were used to identify owners who either served on an advisory board or who currently had one. One sampling of businesses was randomly selected from two local directories catering to small business. Referrals from those businesses were later included in a larger sample. The researcher contacted Small Business Institute instructors, Chambers of Commerce, The Small Business Administration and the Small Business Development Center as well as small business and entrepreneurial consultants.

The sample population was 125 owners. Sixty of those responded with information that allowed use of the data. That was 48% response. Of the other sixty-five, eight phones were disconnected, 36 could not be reached after several attempts (line busy, person too busy to talk, said they'd call back but didn't) and 21 refused to participate.

FINDINGS

In total, the researchers identified 13 advisory boards in SF area and 8 in PS area. Three of the thirteen in the SF area are no longer in operation but were included as useful information sources. The findings to various questions follow:

How familiar with the concept of advisory boards are you?

SF--Either were one or had one, 13 companies plus another five owners who had heard of advisory boards. Forty-two of the owners contacted were unaware of the concept or 70%.

PS--Of the randomly selected group, 9.8% either knew of one or currently use one.

Would you be willing to serve on an advisory board if asked to?

SF--25 yes, 13 maybe, 22 no. Of the 13 already with a board, 12 said yes-- one said "no" due to "lack of time".

PS--54 "yes" of randomly selected group, 46 "no", and two "not sure". Of the eight who currently had boards, seven gave a "yes", one gave a "?" with the notation "conflict of interest".

Other reasons given in SF sample were lack of time, business too competitive, and not sure if qualified.

In the PS group, lack of time was also most frequently mentioned with not sure if qualified also showing up.

In response to how long the business had been in operation when the board started, the responses ranged from with the company since its inception for a thirty year old firm to a twenty year old company with a board that had been in existence for nineteen years before it started aboard. See Table 1).

TABLE 1 AGE OF BUSINESS AND AGE OF ADVISORY BOARD

	SF		PS	
Age of Company	# Co's	Average Age of Advisory Board	# Co's	Average Age of Advisory Board
0 - 5 years	1	3 years	3	6.6 months
6 - 10 years	5	1.65 years	1	4.5 years
11 - 20 years	4	4.5 years	3	2.8 years
over 20	2	14.5 years	1	30 years
TOTAL	12		8	

How many members are on advisory board?

The average number for SF ran from 1 to 25 and in one case up to 35 members. The PS sample ran from 1 to 8 with quite even distribution between 3 and 8 members. The distribution was mostly the same in the SF sample except in the group that had been in business for 11-20 years. The three companies responding there had an average of 13.5 members.

Are members paid?

SF -- Four of the thirteen boards were paid. Three paid less than $100 a meeting. One paid $200- 300 a conference.

PS -- Two of the eight boards are compensated with money. The one larger company with one board member pays less than $100 an hour. The board that has been active for thirty years is paid a fixed hourly rate of $50-100 per meeting. Sometimes the tab is no more than $100-200.

How did you select your members?

SF -- recommendations of others was listed most frequently. Clubs and acquaintances each were mentioned specifically six times. Four had advisors they had met through executive seminars and one person met an advisor through a former classmate. Several respondents suggested relatives, clientele, management consultant referrals, good friends in non competing businesses and SCORE advisors with the Small Business Administration.

PS -- for the most part, board members were selected on the basis of recommendation by acquaintances of the owners or were people with whom the owner had previously done business. One owner used an approach of listing her company's strengths and weaknesses and going about choosing people to fill in the weak spots.

What business experiences do your advisory board members have?

SF -- Answers varied considerably but included: accounting, banking, community business people, political, legal, purchasing, computers, psychiatric, direct mail, production, marketing, sales and strategic planning.

PS -- All of the boards had advisors with very good business experience in the words of the owner. Many of the advisors had small business/entrepreneurship experience. Management consultants with small business experience sat on five of the eight boards. Three owners had other small business owners. Three had advisors who were managers in large corporations, one tapped the advice of a university professor. There were lawyers, serving on four of the boards and an accountant serving on one.

In both cases, SF and PS, there was only one board on which there were advisors who were not deemed to be totally independent.

Other general observations from both samples: Some had written descriptions of ground rules and guidelines for their boards when they began. Most did not. Boards tend to meet more when needed than in an established pattern such as monthly, bimonthly, quarterly or twice a year, there is not usually data provided between meetings .... though the point was made in the PS sample that the owners try to keep their board members informed about the company between meetings. A few boards take minutes and distribute the minutes to the members.

Most used advisory board meetings to discuss issues and problems of a wide nature from items such as new product marketing, business expansion, personnel decisions, tax implications, cash flow, support giving (i.e. informative seminars), changing direction, and management problems.

The meetings are usually chaired by the owner though some groups are chaired by another member.

Benefits of advisory boards in SF and PS sample:

All agreed in general with the value of the advisory board experience except one person in the SF sample whose board was formed too late to prevent bankruptcy. The rest who thought it was a good experience listed such benefits as: good deals and discounted prices, networking to find other clients, developing close friends, broadening general business experience, made better decisions than would have made on own, boards were a source of motivation.

When asked what they could do to improve their advisory boards such recommendations were given as: focus more clearly on goals, more support to keep going, setting specific terms of duty, define the board's function at the start. In both samples advisory boards do not replace boards of directors -- three of the companies in the SF sample had boards and two of the larger companies in the PS sample had boards.

SUMMARY AND IMPLICATIONS

The high failure rate of entrepreneurial and small business ventures is often attributed to lack of managerial skills.

There is firm evidence to suggest that non-paid advisory boards for small business and entrepreneurial start-ups could be definite help in this matter. In the businesses identified in the San Francisco Bay area and the Puget Sound area which use advisory board, the owners profess overwhelming support for the concept.

The experience of serving on an Advisory Board is perceived as beneficial. Business owners, SCORE representative, past Small Business Institute participants, lawyers, accountants, bankers, consultants, college professors, graduate students, managers in larger businesses all seem willing to participate.

What is needed is a vehicle or process to enable entrepreneurs and small business owners to become aware of how to form and effectively utilize advisory boards.

When both the owners and advisory board volunteers receive information and training there will be many more small businesses who will benefit from an advisory board. This will increases the level of community support with everyone gaining. It will help provide the small business person with a longer term source of management assistance. It is expected that these to be formed advisory boards could serve as training grounds for the owners and the volunteers. As the businesses grow, the expectation is that several advisory boards will develop into paid boards of directors.

The author's belief in the implications is supported by recent participation with a group including the SBA in coordinating the formation of twenty-five non-paid advisory boards for small businesses in the King County area. The boards rely heavily on SBI alumni who have responded overwhelmingly positively to participating.

At this point, the evidence is that not many small business owners use non-paid advisory boards. However, if it is possible to double in one year the use of non-paid advisory boards in one county, we suggest that the question of "who uses a board" will be answered affirmatively by an increasing number of small business owners.

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ALCOHOL AND DRUG TESTING IN THE WORKPLACE

Differences in Policies, Practices, and Perceptions of Small vs. Large Companies

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ABSTRACT

One of the most pressing concerns of human resource managers and society in general is abuse of drugs and alcohol. The costs to the employers and society in general for workplace related drug and alcohol abuse are phenomenal. Testing of employees has become a key issue. Twenty-one hundred firms were surveyed to seek out information regarding policies, practices, and perceptions related to drug and alcohol testing. Differences between the response of small and large firms to the abuse problems are noted and broad guidelines for establishing a testing program are provided.

Introduction

Approximately thirty three percent of Americans over the age of twelve have used illegal drugs at some time as compared to four percent in 1962. An estimated twenty two million Americans use marijuana regularly. Employees increasingly use alcohol and drugs at work, arrive for work under the influence, or deal drugs to their co-workers. Resulting problems for employers include hazard to work performance, property and personnel - lost productivity and man hours, poor morale, increasing incidents of theft and accidents, rising insurance costs, escalating litigation and grievance administration expense, and potential employer liability for injuries to workers and the individuals outside company premises. (1)

Drugs and alcohol use by employees is estimated to cost industry as much as $25 billion annually. According to the Employee Assistance Society of North America, the losses to business attributed to alcohol abuse alone include the following statistics: 1) absenteeism among alcoholics or problem drinkers is 3.8 to 8.3 times greater than normal; 2) alcoholics have a two to three times greater risk of being involved in an industrial accident; 3) up to 40 percent of industrial fatalities and 47 percent of industrial injuries can be linked to alcohol abuse and alcoholism; 4) grievance procedures by workers appealing drug or alcohol related firings cost employers an average of $1,050 each; 5) non-alcoholic members of alcoholic families use ten times as much sick leave as normal; and 6) lost productivity due to alcohol and drug abuse costs the United States $39.1 billion a year; of that amount $30.8 is attributed to drug related losses. (2)

In response to the escalating cost and incidents of alcohol and drug related abuse problems in the workplace organizations have with increasing frequency adopted policies and procedures to deal with abuse. Perhaps the most controversial aspect of these policies is the increasingly popular desire to have employees clinically tested for substance abuse. Hardly a day goes by without a report of new controversy concerning the testing of employees for substance abuse.

In an attempt to distinguish the differences between the policies and perceptions of drug and alcohol abuse in the workplace of large and small firms 2,100 businesses were surveyed. Of the 2, 100 businesses queried over 400 businesses replied. The small firms (fewer than 250 employees) provided 260 responses. The large firms (250 or more employees) provided 140 responses.

DATA GAINED

Concern about drug and alcohol abuse was increasing. But it appeared that concern was increasing at a more rapid rate for the large (53 percent vs. 20 percent).

Almost one third of the large firms routinely performed pre-employment drug screening and an additional 30 percent were considering it. Only 7 percent of the smaller companies conduct such pre-employment screening, but 12 percent said they were considering doing so. All but 15 small and 5 large firms said that they would send employees to in house counseling or a formal employee assistance program. Fifty-eight percent of the large companies and 22 percent of the smaller firms had an employee assistance program where workers could either receive counseling to help them overcome their problems or be referred to an outside program. Both the small and large firms stated overwhelmingly that help would diminish if not totally stop after the employees involvement. While large firms tended to have identical policies in regard to drug and alcohol abuse about 20 percent of the smaller firms tended to have harsher policies regarding drug abuse than alcohol abuse.

SURVEY CONCLUSIONS

It is not really surprising that large firms perceived drug and alcohol abuse to be more of a problem than the small. Small firms have more face to face communication, less shift work, more sense of family and thus more hands on data of a worker's condition. Significantly, despite the closeness of the small firm the desire of management to use pre-employment screening was increasing. Thus the growth of the drug problem routinely reported in the newspapers was not an apparition--it was for real.

While the smaller firm is often thought of as "kinder" to its people there was congruence between the small and the large in regard to repeat violators--no tolerance.

While some suspect that small firms personnel policies are primitive they did have about fifty percent of the advanced employee assistance firms as the large--not primitive indeed.

Both small and large firms allowed deteriorating job performance or absenteeism to trigger their desire for testing of those already employed.

It is interesting to note that although the use of testing was increasing, about 35 percent of the respondents (equally proportioned between large and small) expressed concern about the reliability and validity of testing.

GUIDELINES FOR ESTABLISHING A DRUG AND ALCOHOL ABUSE PROGRAM

Careful planning is imperative in the establishment of work rules concerning drug and alcohol abuse, testing programs and/or rehabilitation assistance programs. The planning process should include certain specific steps which will result in an organization specific program and enhance the probability of successful implementation and maintenance of that program.

The suggested approach to program establishment includes the following steps:

1) Direct attention toward the organization's current drug and/or alcohol abuse program. Is there a problem? If so, what is the extent of this problem? In what way does the problem manifest itself. By forcing attention upon the issue, one develops a clear understanding of the current drug and alcohol abuse situation and he/she establishes a rational groundwork for specific planning.

2) Determine your ability and your willingness to develop, implement, and maintain a program which will effectively address the needs of the organization. Provided ability (e.g. sufficiency of human and financial resources) can be established, critical self evaluation will be necessary. Are you willing to sustain the program once it becomes a reality (Having no program is preferable to having one which is inadequate or short-lived)

3) Develop specific program goals. In order to plan an appropriate program, one must possess a firm understanding of what that program is meant to accomplish. Programs will vary according to goals.

4) Plan an alcohol and drug abuse program which is appropriate for your organization. Specific inclusions will evolve freely if goals remain in sight. It is not advisable to merely adopt a program which is used by another organization. Although it may be helpful to investigate the variations and the success of other existing programs, the program that you ultimately establish must be tailored to your specific situation and goals.

5) Examine the legal implications of your proposed program. Be certain that you understand the potential significance and potential ramifications of the actions that you plan to take. Seek legal advice so that you can become aware of statutes with which you must comply, potential grounds for litigation and the industrial relations implications of the proposed program. A re-evaluation and redesign of the proposed program may be indicated.

6) Determine the potential effect of your proposed program on other organization goals. Will the goals of the alcohol and drug abuse program conflict with or enhance other goals? For example, how will it effect goals involving employment relations? How will it affect employee morale? Objectivity is imperative if one is to realistically analyze potential effects on other aspects of the organization and its culture.

7) Proceed with implementation only if you are satisfied that it is indeed appropriate and in the best interest of your organization. Do not over-react. Careful analysis of your unique needs and goals is imperative if a plan is to be developed and implemented.

Drug and alcohol use/abuse programs are becoming increasingly important. If a business owner feels that a program may be of value or of necessity to his/her particular organization, steps toward implementation must be taken with caution. Objective evaluation, planning, and development and the assistance of a competent attorney are key to the establishment of an effective employee drug and alcohol abuse program.

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CAN SMALL BUSINESSES BE COMPETITIVE SERVING GEOGRAPHICALLY DISPERSED TARGET MARKETS?

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ABSTRACT

Many small businesses face the problem of effectively serving geographically dispersed target markets. They face competitors that employ field sales and customer support, personnel to cater to the needs of the customer base. The cost of selling appears prohibitive. Yet, even with a superior product offering, it is difficult for the smaller business' to compete through the mails or on the telephone with the personal visits made before and after the sale. The objective of this paper is to explore ways smaller businesses can provide a competitive service level at the lowest possible cost.

INTRODUCTION

This paper will first examine the theory behind traditional approaches to field sales and customer support. Such operations are expensive and have long been subject to value analysis in one form or another. Next, the paper will compare the theory to present practices to derive implications useful for smaller businesses desiring to compete in geographically dispersed markets. Preliminary findings of an ongoing study by the author will provide support for insights concerning present practices. The paper will conclude with a discussion of directions for further research.

The Theory Behind Traditional Approaches

Managers have long faced the problem of how to motivate and direct the performance of their field personnel. Maintaining the productivity of product work groups that include such personnel is a key part of the industrial logistics challenge. Arthur Laufer suggests that logistics should be viewed as an enterprise subsystem concerned with the interrelated activities of operations, marketing, and transportation subsystems. (109 p. 435) The goal is to provide the desired level of service at the lowest possible cost. Determination of the service level is the most important measure of effectiveness of the logistics system. It is the prime productivity measure. In this context, a good logistics information system is required to permit the coordinated action of the various segments of the logistics system. This specialized information system needs to be linked to the larger company system. Laufer points out that typically enterprises have tended to view logistics activities as individual functions to be controlled separately. In the present context, for example, making travel arrangements for a salesperson might be delegated entirely to a travel agent, with changes in schedule negotiated on the fly by the agent and the salesperson. The receptionist might take incoming messages. The secretary for the sales area might send out information brochures only when requested by the salesperson. Accounts receivable may have to approve all new orders before contracts can be signed. Production might specify delivery schedules. The shipping department might determine mode of delivery.

Laufer stresses that such an approach should be viewed with caution. "Since all of the elements... are interrelated it is difficult to achieve efficiency by this sort of subdivision. There are numerous ways in which the logistics function can be organized, but no single form can be designated as best. The important thing is to view logistics in the systems concept, and consider all of the components of logistics as an integrated whole. Only then can any assurance be given that the logistics function will be carried out effectively. All the components can then be coordinated in such a manner as to achieve the objective of getting the output to the user when, where, and how it is wanted, and at the lowest cost." (10, p. 433)

Once it is clear how all the subsystems contribute to the product, including logistics, value analysis can be applied to provide a competitive service level at the lowest possible cost (i.e. reduce the cost of the desired product/service level by examining the specifications and design of the item itself and of the process by which it is sold and gotten to the customer). Industrial dynamics, for example was developed to study, "the information-feedback characteristics of industrial activity to show how organizational structure, amplification (in policies), and time delays (in decisions and actions) interact to influence the success of the enterprise." (4, p. 13)

Similar advice is available from experts in Sales Force Management. Gilbert A. Churchill, Jr., et al. stress that the sales organization should serve three purposes: "1. Activities should be divided up and arranged in such a way that the firm can benefit from the specialization of labor. 2. The organization structure should provide for stability and continuity in the firm's selling efforts. 3. The structure should provide for the coordination of the various activities assigned to different persons in the sales force and different departments in the firm.," (11 p. 104) These experts are sensitive to issues of organizational design such as when to use staff specialists and how to define the chain of command in terms of number of management levels, span of control and authority. They recognize that, "the activities of the sales force must be integrated with the needs and concerns of customers, ... the firm's selling activities must be coordinated with those of other departments such as production, product development, logistics, and finance. Finally, the firm divides its selling tasks among specialized units within the sales force, all those tasks must be integrated." (11 P. 106)

Churchill et al. discuss two concepts, team selling and coordination of organizational design that apply to the present article. "In firms where sales-related functions (installation and maintenance, order processing and expediting, credit, etc.) do not report directly to the sales organization, team selling is often a useful means of coordinating such functions -- at least when dealing with major customers where the cost of such an approach is justified. Although the account manager has no formal authority to control the actions of team members from other departments, he or she can coordinate the team's activities at the field level." (11 p. 125) "One major disadvantage of a team selling approach is its high cost in time and personnel. It also presents a major problem of coordination. Unless the selling efforts of all team members are carefully integrated, conflicting impressions may be given to various members of the customer's organization. Team selling is appropriate for the very largest customers... Although team selling is usually used to win new accounts, it is sometimes also used with lower-level personnel for maintenance selling. Production schedulers, expediters, and shipping personnel may join the sales team to keep an existing account satisfied." (1, P. 126) Theory vs. Practice

The above theory can be compared to present practices to derive implications useful for smaller businesses desiring to compete in geographically disbursed target markets. Preliminary findings of an ongoing study by the author provides some insights concerning present practices.

Study Procedure

The preliminary findings referred to above are based on the results of structured interviews of those who work frequently in the field in sales, sales management, and follow up customer support roles. Ultimately, sample interviews of such personnel will be drawn from a number of industries. The findings used in this paper are derived from over 100 interviews of individuals working for two closely related industries: computer hardware/data communication and computer software. These industries were selected for initial examination because their field personnel could be expected to be aware of the possible use of modern telecommunications and computer links to maintain service levels in the field, as well as more traditional techniques. Populations were made up of companies listed in the appropriate volumes of Data Sources (2). Two initial random samples of 20 each were selected from these industries to conduct an initial field test of the questionnaire. All interviews were conducted by telephone. One frequent traveler was interviewed at each company. The questions tested are listed in Exhibit 1. The purpose of the initial field test was twofold: (1) to set sample sizes for the full study of each industry, and (2) to suggest checklists for each question, based on response frequency, which interviewers could then use during future interviews to expedite recording of responses. The objective was to determine the sample size necessary for each industry to be 95% confident that the population parameters were within +.10 of the sample population (sampling by attributes) (3). It was expected that the sample size implied would be large enough to reveal major trends, and small enough to permit efficient use of interviewer resources. Yes/no responses to question six were used for sample size calculation. The required sample size for software companies was determined to be 66 drawn randomly from a total industry population of 1,924.

To date all interviews for the software company sample have been completed. Exhibit 1 provides a summary of survey responses for this industry. Exhibit 2 explains more about the sampling procedure and analyzes the adequacy of initial survey results.

In addition to the forty field test interviews and the sixty-six interviews from the software industry, background was obtained from interviews with key executives from major lodging providers, managers of executive suites (shared office space and services), office space developers (branch offices), and suppliers of telecommunications and computer equipment. Selection of respondents for background interviews were based on respondent expertise rather than on random chance.

EXHIBIT 1

QUESTIONS TESTED AND SUMMARY OF SURVEY RESPONSES 1. When you leave your company and go on business trips do you notice any change in your productivity?

Fifty-five respondents (83/10) noticed a change in productivity.

2. Does it increase or decrease?

Of those who noticed a change in productivity, 23 (42%) noticed an increase, 21 (38%) a decrease, and 11 (20%) preferred to answer both an increase and a decrease.

3. If it changes, what are the more important reasons why?

No single answer dominated the reasons given for decreased productivity. Most frequently mentioned reasons for a decrease were wasted time during travel (both inherent and due to mix-ups in arrangements), fatigue or stress related to travel, and lack of coordinated access to telephones and other office support such as customer records and data. Seventy percent of those who felt productivity increased explained it was because face-to-face contact with customers while on travel allowed them to build a rapport that made it easier to meet customer needs and close sales. About half of those who felt productivity increased stated a contributing factor was getting away from office and home routine/distractions which allowed them to focus on their work. Of those who perceived both an increase and a decrease, most saw the increase due to face-to-face customer contact. Decreases were due to fatigue; neglected office planning and paperwork; and, in a few cases, neglect of customers not visited during the trip.

4. What is the single biggest obstacle you experience in doing your job well while you travel?

Only one respondent did not have a ready answer for this question. A few stressed more than one obstacle. Most responses had to do with time wasted while traveling. Obstacles such as time lost while on planes, delays in flights, inconvenient connecting flights, deadtime in airports, ground transportation problems and getting lost were mentioned 45 times by the 66 respondents. By contrast, fatigue and stress were mentioned only 6 times, in response to this question. Office related efficiency issues such as access to customer data, communications equipment, support staff, or other resources were mentioned 20 times. Most of these latter obstacles were related to communicating current information back and forth between the person in the field, home office and the customer, as opposed to the type of office routine.

5. What is the single most important thing your company does for you while you are traveling that boosts your productivity?

Over 80 "most important" things were stressed by the 66 respondents. Of these, five were mentioned frequently enough to be considered significant. Providing a message base (a simple answering service) was mentioned 18 times. More extensive phone support (answering routine customer questions and putting through orders) was mentioned 17 times. More sophisticated telecommunications support (voice mail, call forwarding/message relay, and data transfer) was mentioned 16 times. Functions that could only be performed by an informed administrative assistant or sales associate were mentioned 19 times. Finally, efficient handling of travel/entertainment expenses were mentioned 9 times.

6. Imagine you are King (Queen) for a day and could ask your company for anything you needed to improve your productivity while you travel. Would you request better access to any of the kinds of things we take for granted while we are in the office such as types of people (support staff), facilities, equipment and services?

7. If yes, what are the most important things you need better access to to improve your productivity while on business trips?

Ninety-two percent of respondents wanted better access to office resources while an travel. People ... Executive secretarial assistance and technicians were ties for most frequently mentioned (20 times each). Not necessarily significant to this question, but still of interest overall , were 7 requests for more access to top management for quick decisions and 6 requests for administrative assistants/junior partners. Facilities ... This type of resource was only mentioned 9 times. Six requests were made for use of a private office while in the field. Equipment ... A variety of equipment needs were mentioned ranging from better telephone service to access to corporate jets! Most requests centered around improving communication. Twenty-five wanted a personal computer (presumably portable). Twenty-one specified a modem or other communications link available for extended hours. Services ... Thirty-four responses requested a variety of services. No one service dominated the responses. Ten had to do with constant communication ability by modem or other means. Seven requested help with scheduling or rescheduling appointments. Five had to do with routine secretarial duties and four had to do with travel arrangements.

8. Have you ever changed job or company because you received inadequate support for your work during business trips?

9. If yes, what kind of support was lacking?

Only 10 of the respondents (15%) indicated they had changed companies because of inadequate support. No single reason was significant.

10. Which of the following best describes your position?

Thirty-three (50%) indicated sales was at least part of their job. Twenty-two (33%) described themselves as management. Eleven (17%) held staff positions (customer service, technical support, etc.).

EXHIBIT 2 ANALYSIS OF INITIAL FIELD TEST OF FREQUENT TRAVELER QUESTIONNAIRE

Sampling procedure--The initial field test of the questions in this exhibit was conducted in April, 1986. Sampling by attributes was used (95%) confidence + 10% on Question 6. Software companies selected had to have greater than $1,000,000 in sales. Attempts were made to interview one frequent traveler at each company selected, but a maximum of two call backs were permitted before dropping the company from the sample. Potential respondents were asked how many business trips they made during the last twelve months and how many nights they stayed in a hotel/motel on business during the same period. If either answer was less than five, the respondent was disqualified and another respondent that did qualify was sought within the company.

Analysis of sample adequacy--Fifty percent (33) of respondents indicated sales was at least part of their job. An additional thirty-three percent (22) described themselves as management. Seventeen percent (11) held staff positions (customer service, technical support, etc.). The sample differs in several ways from the typical frequent traveler depicted by a 1985 lodging survey (9):

Lodging Lodging Sample Survey Sample Survey

Age<35 41% 28% Income <20M$ 3% 16% 35-50 52% 42% 20-29 9% 18% 50+ 7% 30% 30-49 36% 40% 50+ 52% 26%

Sex M 77% 64% Nights 5-10 11% 10% F 23% 36% 11-20 23% 31%

Trips 5-10 33% 63% 21-30 15% 21% >10 67% 37% >30 51% 38% Mean # 25 14.6 Mean # 54 36

The present sample is by in large younger, more affluent and travels more frequently than the typical frequent travel depicted in the 1985 lodging survey. Females in the sample are somewhat underrepresented. All except the latter might be expected given that software companies were surveyed. Actual dispersion on Question 6 (and Question 2 for that matter) suggests that sample size was more than adequate.

Field work to date and the initial results from software companies make it appear that present practices among companies with sales over $1,000,000 leave room for the well organized smaller business to compete. (See Exhibit 1.) It also appears these barriers are well known both by those who work in the field and those who serve them. The reasons stated for decreases in productivity are partly unavoidable. Many, however, probably have to do with inadequate trip planning and the need for more effective personal time management. The key point is respondents seem to accept the delays and problems as given. Few had any suggestions about how to deal with this issue beyond having some other person or service take care of travel arrangements and schedule planning. This leaves room for competition. On the other hand, it is clear that many respondents feel face-to-face contact with customers remains vital to close sales. Telecommunications does not yet substitute for this contact and the smaller company cannot plan around the necessity for travel -- at least in the software industry.

A careful review of responses to questions 4 and 5 suggests telecommunications support is very helpful to those in the field. The more that those who answer the telephone know about the business of those working in the field, the easier it is for the person in the field to maintain productivity. This implies that a smaller business can gain most of the advantages enjoyed by field personnel in large organizations by setting up "teleservice" teams that link field personnel to home office personnel, as opposed to relying on the traditional receptionist or answering service.

The key to competitiveness appears to be in the provision of continuity. Many larger firms still tend only to offer their field personnel business services at fixed locations. They do not provide enough continuity. They do not know the field person's business well enough and do not continually assist the field person as he/she crosses the country. (Interestingly, this can be the case even if travel is exclusively between branch offices across the country.) It appears so far that, in order to work effectively in the field, field personnel need support from a channel manager (or channel team) that is knowledgeable about the details of the traveler's business. In some regards this channel role is one of an executive assistant. In other regards it is similar to the role of account manager who supports sales by expediting and coordinating between subsystems. Duties of this role mix specialized staff function with integrating and coordinating. Duties include: 1. Expediting constant, two-way telecommunications (screening calls, handling the routine, and forwarding the important). 2. Scheduling and rescheduling appointments and handling the corresponding travel arrangements. 3. Expediting data base access, particularly of prospect files, and 4. Obtaining timely approvals at the home office for commitments being negotiated in the field.

The encouraging part for smaller businesses is that the cost of providing such continuity need not be prohibitive. Assuming that the smaller concern has not taken on a larger market than it can possibly handle, one can visualize a competitive "teleservice team." At least five alternative approaches can by employed to deal with the problems noted by frequent travelers. (Exhibit 3)

EXHIBIT 3

ALTERNATIVE APPROACHES TO MAINTAINING COMPETITIVENESS IN GEOGRAPHICALLY DISPERSED TARGET MARKETS

1. Telecommunications Focus--Install the necessary hardware and personnel to create a constantly assessable two-way communications line with the home office (24 hours a day). The home office message base would focus on message taking, call forwarding and voice mail. Field personnel would have their telephone credit cards enhanced with beepers and cellular telephones in areas where such services were available.

2. Teleterminals--Expand on the first alternative by providing two way data transfer capability including electronic mail. Proper password security and archiving of key correspondence would permit authorizations of field commitments over telephone lines.

3. Channel Managers--Establish a channel manager in the home office to handle messages, scheduling and approvals from other subsystems without committing to extraordinary telephone or data communications capabilities.

4. Channel Managers + Telecommunications--Expedite the channel manager's role by overcoming some of the logistical problems with better two-way telecommunications.

5. Channel Managers + Teleterminals--The ultimate linkage permitting both voice and data transfer during teleconferences.

How to be Competitive - Weighing the Alternatives

Each of the five options listed in Exhibit 3 has its costs and benefits. Study results to date indicate that more efficient two-way telecommunications (Option 1) is perceived as a top priority. Indeed, the whole field of telemarketing has been developed to gain sales cost efficiencies in this area. (11, pp. 50-51) Inside telephone salespeople and outside field salespeople are used to accomplish different selling objectives. The inside salespeople tend to focus on prospecting, servicing existing accounts when unexpected problems arise, seeking repeat business from small existing accounts, and getting the word out about new developments. The relatively expensive outside sales force concentrates on activities with the highest potential long term payout like developing major new accounts, providing customer instruction, and personal on-site service. (As Mack Hanan would describe it, they practice consultive selling. (8)). Inside and outside selling are two different types of selling activities. Each may require different policies and procedures and compensation. This increases the complexity of the selling subsystem. Still, there is a definite trend towards acceptance of inside selling--both by selling organizations and customers--as more efficient in the use of everyone's time. (12, p.104) The same trend is seen by experts in customer relations. (7) The toll-free 800 number affords a tremendous increase in direct customer contact. Customers are being reached that have not been reached before--both before and after the sale. Results have been positive for many companies, as long as trained staff are available to use the increased telecommunications capabilities to advantage.

Increased productivity from improved two-way communications is contingent upon proper procedures to screen calls and expedite action on incoming calls. Otherwise, one suspects field personnel would end up receiving many expensive, low priority calls while on travel. Also they would still have to play telephone tag with resource people at home office when approvals were needed for field commitments. This option also does little or nothing to deal with the appointment scheduling and travel arrangement problem. This option also has implied staffing costs in terms of increased operator training requirements and required service. Required training for field personnel would be relatively small.

The second alternative (even more costly than the first), assuming a distributed processing approach is used, would permit access by field personnel to home office files and provide a more expeditious way to allow the field to get approvals. Messages on leads could be sent and received, telexes dispatched, letters sent overnight on company stationary and prospect lists created and maintained. It would also permit more efficiency in do-it-yourself rescheduling and travel arrangements by those in the field. The state of the art, recently described by Judy Getts, would combine a portable computer, communications software, and electronic mail service such as MCI mail. (5) Getts' article implies that the skill levels required of operators would definitely increase. At the hub of the network in the home office, increased system administration skills would be required even if a service like MCI mail was used instead of an in-house mainframe to handle electronic mail. In the field, all personnel would have to be trained to use the equipment and communications software. Even the hardware costs of this option add up to more than they first appear because of the need for local intelligence and the need to make hard copies of key documents while in the field.

The third alternative would create a level of bureaucracy which is hard to define in terms of traditional organization charts. As noted earlier the channel manager role is similar to the account manager role used in field sales organizations. This position works for the field personnel rather than supervising them, handling myriad details. In this sense the job is like that of an administrative assistant. The position also acts as a liaison within the marketing subsystem and interfaces with other subsystems. There is a good probability that such a role could mitigate most of the expressed productivity barriers faced by field personnel. However, without an efficient telecommunications or teleterminal system, the number of field personnel each channel manager could service may prove too small to be cost effective. As noted earlier, experts have found team selling to be relatively expensive and have reserved this option for large accounts.

The fourth and fifth options provide telecommunications interfaces to the selling team. On the one hand the technology would allow the selling team to broaden its span, particularly if the channel manager role was mixed with both inside and outside salespersons. On the other hand, as the network grew specialized staff would have to be added to administer the system and training requirements for all personnel would increase. It would be harder to develop and maintain depth, for each team position. The potential payoff from each outside position would have to be relatively high to justify establishing it and linking it via phone lines to an in-house network or to a electronic mail service. This is probably why a recent survey of Goodmeasure, Inc. of American Management Association members reveals that of the ten percent of employers in the sample that permitted work-at-home arrangements, only about one-fifth had hourly or clerical/secretarial employees participating while almost two-thirds had professional staff participating. (6, p. 47-48)

The Most Promising Solution

Reviewing the above options, Pareto's law dictates that once the critical few problems are handled, the extra cost of handling the numerous remaining, relatively trivial problems will not be worth it. Picking the best alternative for smaller businesses to use to compete in geographically disperse target markets is contingent on a number of factors.

Clearly the nature of the company's market, its products and services, and its geographic scope, will impact the final choice. Still, larger firms experienced in working in the field have been coping with the tradeoffs for a long time. The problems they still face and the trends solutions have taken are becoming clearer as the present study progresses.

What appears practical for the smaller business? Team approaches with membership both inside and outside the home office have historically worked well, but been expensive. Telecommunications improvements have justified adding inside selling (telemarketing) and customer support to the team -- developing a "teleservice" team. This mix of sales contacts are more efficient for both the seller and the buyer. But what about high technology solutions for field personnel? It is not at all clear that teleterminal options, with their system administration requirements and field complexity, can yet simply be assumed to be cost effective. The state of the art of networking geographically dispersed, intelligent workstations is not sufficiently advanced to make this option cost effective except for high payoff outside positions such as consultive selling to major accounts. Even in such special cases, careful planning of the work to be done in the field and team work on dealing with events that occur while the employee is in the field are what is needed to overcome the difficulties articulated by respondents. Today, the choice would seem to be channel management that takes advantage of modern telecommunications technology to reduce coordination costs.

In summary, the solution for the smaller business that wants to compete in geographically dispersed target markets is a people solution, more than a hardware solution. For the near term, it will be based on building teams of inside and outside personnel that use careful planning and improved telecommunications to achieve acceptable service levels for larger numbers of clients. The critical success factor is effective management of the channel team. The ability to put together and effectively manage such a teleservice team is not the exclusive province of big business.

Directions for Future Research

The study discussed in this article is an ongoing one. Many more field personnel in many more industries remain to be interviewed before the initial results discussed in this article can be considered definitive beyond the software industry. The workability of the solution suggested for smaller businesses that wish to compete in geographically' dispersed target markets depends on the degree to which full communication can occur between team members. Attention will have to be given to the special problems and opportunities of the team building process in smaller businesses and to whether or not channel managers can maintain morale via telecommunications and computer links when the channel team is small and spread thin. It is certain the process will have to be managed to succeed. The research challenge is to determine the management mix required be competitive and to determine whether or not smaller businesses can use new telecommunications technology to affordably reach the necessary service level. REFERENCES

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EMPLOYEE SELECTION FOR SMALL BUSINESS OWNERS: THE INFLUENCES OF THE UNIFORM GUIDELINES AND COURT DECISIONS

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ABSTRACT

The Uniform Guidelines on Employee Selection Procedures (1978) were promulgated with large businesses in mind in order to affect large numbers of employees as rapidly as possible. However, the employee selection validation procedure advocated by the Equal Employment Opportunity Commission, criterion related validity, is one that small business owners are unable to use due to statistical restraints and the lack of personnel with the esoteric knowledge of validation proce-

dures. These restrictions, coupled with court decisions such as Albemarle Paper Company v. Moody in which the United States Supreme Court ruled the test validation guidelines issued by the EEOC were to be given "great deference" by lower courts, have left small business owners with one practical and potentially legally defensible approach to employee selection. This paper briefly mentions the advantages of valid employee selection procedures, followed by a detailed description of the Uniform Guidelines on Employee Selection Procedures (1978), relevant court cases, and a case study describing the validation of a small business employee selection test by the author.

INTRODUCTION

The importance of small business to the U.S. economy was well summarized by Siropolis (1986), who wrote:

... more than 99 percent of the nation's 16 million businesses are small-even if we define a small business as one that employs fewer than 100 rather than 500 .... Further evidence of its vitality is the fact that small business employs roughly half of the nation's workforce (pg. 8).

In addition, Siropolis (1986) listed numerous other reasons for the importance of small business to the U.S. economy, such as the higher return on equity small manufacturers earn than large manufacturers, the innovation found in small businesses as evidenced by small businesses accounting for half of all major inventions in the last 30 years in the U. S., and the dependence of large businesses on small businesses as both suppliers and purchasers. These economic facts indicate that small business in the U.S. is the paramount force for economic growth and the creation of jobs, as noted recently: Small businesses are the principal job creating sector of the economy during recessions and expansions" ("The State Of", 1985, pg. 246). Further evidence of the economic importance of small business has recently been published:

Employment gains in small-business dominated industries in construction (18.9 percent), finance, insurance and real estate (12.7 percent), and services (12.6 percent) are impressive when compared to the gains made in similar, large business dominated industries. In construction, the small business ted industries had employment gains of 18.9 percent, while the large business industries showed an employment loss of 10.6 percent. The relative strengths of the small business gains in wholesale and retail trade are also significant ....Small firms with fewer than 100 employees... generated 52.6 percent of net employment growth from 1976 to 1982.

("The State Of", 1985, p. 17-21). One can add to this the reliance of the U.S. government on small businesses, as evidenced by the federal government purchasing almost 29% of its of goods and services from small businesses in 1983 ("The State Of", 1985).

EMPLOYEE SELECTION

An area of vital importance within small business management is the area of employee selection. An increasing awareness of the importance of employee selection has been noted: "Nearly 40% of surveyed employers are using more prehiring testing of job candidates than they were five years ago" ("Prehiring Tests", 1986, p. 17). The importance to the U.S. economy of employee selection in a small business is due both to the fact that small businesses create the majority of new jobs in the U.S. (Birch, 1979; "The State Of", 1985), and the impact of the employee selection process on a small business. First, the results of a valid selection procedure include increased productivity of as much as 20 percent (Schmidt, Hunter, McKenzie, & Muldrow, 1979). This is an important result to small business owners, as productivity improvement has been rated as the number one concern of both CEOs and executives and engineers in separate surveys ("Productivity: A Top", 1986, p. 46). Other important results include an avoidance of lawsuits (Dreher & Sackett, 1981; Kleiman & Faley, 1978), greater job satisfaction and organizational commitment, reduced absenteeism and fewer disciplinary actions (Fear & Ross, 1983), reduced time spent in supervision for the small business owner, and reduced training costs and turnover (Stone & Ruch, 1974). The potential for reduced turnover is also important for small business owners, due to recent data indicating that:

Small businesses have higher annual employee turnover than large companies. The Administrative Management Society reports that businesses with 26-250 employees have a 19% turnover rate, while larger firms (more than 5000 employees) average only 7% ("Small Businesses, Turnover" 1986, p. 13).

In total, these results are particularly important due to the greater relative effect each employee has in a small business as opposed to the effect of an individual employee in a large business.

In the U.S., the employee selection procedures used by all business owners are regulated by the Uniform Guidelines on Employee Selection Procedures (1978). The Uniform Guidelines (UG) were designed to provide technical assistance to employers and were written following a review of relevant court cases and consultations with industrial psychologists. At present, the UG are serving as a reference for determining the legality of currently used selection tests. The UG are administered by the Equal Employment Opportunity Commission (EEOC), which is empowered to do so by Title VII of the Civil Rights Act of 1964. As Landy and Trumbo (1980) have noted: "The EEOC has evolved from a weak public advocate status to a strong and active enforcement agency, with broad powers to initiate and negotiate legal and administrative action on behalf of protected minority groups" (p. 92). Although the UG are not "law" as a lawyer would define law in that they were not passed as bills in Congress, they are frequently referenced as technical guides by judges. In the UG, the employment decisions made by business owners and managers are regulated and broadly defined, e.g., promotions, referrals for training, as well as selection for hiring are all subject to the influence of the UG.

The UG list three allowable approaches to validating a selection test used by a business. Briefly, criterion related validation approaches focus on the statistical ability of the selection test to predict the criterion, or as noted by Dreher and Sackett (1981): "...criterion-related approaches focus on the relationship between a hiring requirement and job behavior" (p. 552). Another way of describing criterion-related validity was written by Landy and Trumbo) (1980): "When we are investigating the validity of a selection procedure using a criterion related design, typically, we are looking for a significant correlation between a test (predictor) and job behavior (criterion)" (p. 70- 71). The UG define criterion related validity in this way: "In criterion related validity, a selection procedure is justified by a statistical relationship between scores on the test or other selection procedure and measures of job performance" (P. 38292, Federal Register, 1978).

According to the UG, the requirements of the job analysis, which is a comprehensive definition of the tasks performed by a job incumbent, are: "There should be a review of job information to determine measures of work behavior(s) or performance that are relevant to the job or group of jobs in question". The paramount difficulty with conducting a criterion related validity study for the small business owner is the required number of hirees, which is discussed in the UG under the term of "technical feasibility". Although the minimum is not specified in the UG, an absolute minimum is 30 employees (Heneman, Schwab, Fossum, & Dyer, 1986). For many small business owners, this minimum number is more employees than they hire in a year, which in turn makes the criterion related validation approach of little value. In addition, the statistical measures required by the criterion related validity approach are often recondite for a small business owner.

Construct valuation approaches attempt to measure an applicant's amount of psychological characteristics such as "need for achievement". The UG discuss construct validity in this manner: "Construct validity involves identifying the psychological trait (the construct) which underlies successful performance on the job and then devising a selection procedure to measure the presence and degree of that construct" (p. 38292, Federal Register, 1978). The construct validity of a test refers to the extent to which it measures the construct it is supposed to measure. Landy and Trumbo (1980) noted: "It is the most theoretical of the definitions of validity, since it is concerned with the abstractions used in referring to psychological structures, functions, or traits, rather than to the prediction of some external criterion" (p. 73). The job analysis for a construct validity study involves a list of critical job behaviors and the constructs believed to underly the behaviors. These studies are difficult to do, as a "construct" is a hypothetical attribute of a person that underlies and guides their behavior.

Content validation approaches are concerned with the job relatedness of the selection test rather than a concern with the criterion. Landy and Trumbo (1980) defined this approach toe employee selection procedure validation as: "Content validity is concerned with the extent to which the sample of items in a test (and the sample behavior elicited by these items) is an unbiased representation of the domain (i.e., attribute or trait) being sampled" (p. 71). According to the UG: "A selection procedure can be supported by a content validity strategy to the extent that it is a representative sample of the content of the job". An important concept for a content valid selection procedure is the job analysis, which was defined by Schultz (1978): "The purpose of the job analysis is to describe, in specific term, the precise nature of the component tasks performed by the workers on a particular job" (p. 76). A job analysis can be approached in a variety of ways, as noted by McCormick and Tiffin (1974): "Job analysis can be considered as embracing the collection and analysis of any type of job related information, by any method, for any purpose" (p. 49). The job analysis for a content validity study involves interviewing and observing incumbents:

Job analysis for content validity. There should be a job analysis which includes an analysis of the important work behaviors(s) required for successful performance and their relative importance and, if the behavior results in work product(s), an analysis of the work product(s). Any job analysis should focus on the work behaviors and the tasks associated with them ... The work behaviors selected for measurement should be critical work behaviors and/or important work behaviors constituting most of the job.

The key to content validity is the answers to the questions the small business owner must ask: "How representative of on the job behaviors is the test? Does it sample all important aspects of the job?" Landy and Trumbo (1980) wrote "Content validity is determined on the basis of how well the test material samples the job performance domain" (p. 72). The validity of a content validation study is judgmental; no statistical analysis is done (Robinson, 1981).

The value of the content validation approach to a small business owner is that it allows a selection test to be validated within the UG restraints, and at the same time it does not require large sample sizes or recondite statistical analyses:

When is content validation appropriate? One circumstance is when there are too few people available to form a sample for purposes of empirical validation. While there are differences of opinion on what the minimum necessary sample size is for empirical validation, an absolute minimum is 30 individuals who all perform the same job (Heneman et al. 1986, pg. 281-283).

The restrictions of the content validity approach are few. One of the restrictions is that the selection test should consist only of knowledge or skills that cannot readily be learned on the job (Miner & Miner, 1980). In addition, content validity is prohibited by the UG to measure mental processes as part of a selection procedure.

An example of the content validation approach to employee selection is the appropriately titled Content Oriented Personnel Selection in a Small Business Setting by Robinson (1981). In his article, which involved the content validation process needed in designing a selection procedure which was used to hire one construction superintendent for a small construction firm, Robinson (1981) informs the reader of the steps necessary in a job analysis for a content valid selection test:

1. Convene a panel of experts.... 2. Ask the panel to identify all the broad objectives to be met by an ideal incumbent on the target job. If objectives can be so quantified that they can properly be called standards, so much the better.... 3. List specific behaviors required to meet each objective .... 4. Identification of "critical" tasks ... The content sample will be valid to the extent that the critical tasks reflect actual job performance .... 5. Determination of interjudge agreement as to the importance of major dimensions of the job... (pgs. 78-79).

The importance of such a systematic approach to the job analysis was emphasized by Dreher and Sackett (1981): "The quality of any content validation effort depends on the thoroughness and appropriateness of the job analysis" (p. 554); the job analysis will be used to determine if the content valid test actually samples relevant job behavior mentioned in the job analysis as important. Having conducted the job analysis, Robinson (1981) constructed a test battery based upon work sample procedures. As an example, the applicants were given a construction error recognition test in which the applicants were required to inspect a 8' by 12' shed that contained 25 construction errors. The applicants were to list the construction errors they spotted during their inspection.

This emphasis on the UG when discussing employee selection approaches for small business owners stems from two major court cases which directly ruled on the use of content validity as a way of validating a selection instrument. In Firefighters Institute for Racial Equality v. City of St. Louis, a promotional examination for fire captains was ruled to have adequate content validity within the directives of the UG. In U.S. v. Connelie, a selection procedure for New York State Police was ruled to be invalid due to in large part the lack of a task-oriented job analysis nor was the frequency and importance of job duties identified. In both of these cases, the UG used in making the judicial rulings.

Two other court cases which indicate the importance of understating content validity are Harless v. Duck and King v. New Hampshire Department of Resources and Economic Development. In Harless v. Duck, a structured oral interview was found to be rejecting more female applicants than male applicants, however, the employer argued the interview had content validity in that hypothetical situations were used that a police officer might actually face. The court ruled the selection interview was valid, in large part due to its content validity. In King v. New Hampshire, a business lost a discrimination lawsuit due to applicants being asked questions which were not job related, i.e., not based on a job analysis and therefore not content valid.

With the importance of employee selection validation in mind, coupled with the feasibility of the content validation approach for small business owners, I would like to describe the approach I used for a small business owner located in the Midwest.

The small business is a general purpose real estate office ("general purpose," in the sense that it handled farm, commercial, and private dwelling real estate sales) which has two owner managers and 10 sales associates. The primary function of the sales force for this small business is to sell as much real estate as possible, in terms of monetary value rather than number of units sold. The organization did not have a job analysis of the job of real estate agent and was using an unstructured interview to hire applicants.

The initial step was to develop a job analysis. The purposes of the job analysis were to (a) define the job duties being performed by the job incumbents, (b) obtain a listing of the requisite knowledge, skills, and abilities to perform each job duty, and (c) determine the importance and time spent on each job duty as perceived by the incumbents. For this small business, the process of collecting information for the job analysis consisted of three steps: (a) reviewing the appropriate entry in the Dictionary of Occupational Titles, (b) reading the job related material from the firm's files, and (c) a series of interviews with all 10 real estate agents and both of the owner-managers.

Due to the job analyst's lack of familiarity with the job, the first step was to review the job description in the Dictionary of Occupational Titles. Its value is noted by Bass and Barrett (1981): "The job analyst can turn to the Dictionary of Occupational Titles to get a concise definition of almost any job in American industry" (p. 238). The use of this volume when approaching a job one is not familiar with was also noted by Cascio (1978): "First, the reader can become familiar with the vast array of jobs in general and with appropriate terminology in each job, (p. 147). The second step also involved acquiring some job related information about being a real estate agent; this step consisted of a reading of the informational and training manuals that are made available to the real estate agents. The perusal of these manuals was valuable in giving the job analyst background information necessary to conduct the third step of the information collection, the interviews with job incumbents. These interviews were conducted in a private room and ranged from 30 to 90 minutes. The interviews followed a patterned interview form, as recommended by Cascio (1978). The interview questions asked for traits, behaviors, and knowledge that the incumbents deemed necessary for the completion of the job of real estate agent. The interviewees were also informed that any knowledge or behaviors an applicant could learn within eight hours was not to be included. An example of an interview question is "What is the order of behaviors from the time you contact a customer until you are through with a sale?" The interviews generated a list of 106 job duties.

Each of the interviewees received a copy of the 106 job duties, along with an instruction sheet asking them to rate each item as to its importance to their job and the relative amount of time they spend performing that job duty. The mean rating given each of the 106 job duties was computed by the job analyst for both the rating dimensions.

With the interview information and summary statistics on hand, a selection instrument was constructed which was based on job duties which were rated highly in terms of their importance and time spent on each of them by job incumbents, and which job incumbents considered were not trainable within eight hours. The selection instrument was based on a job sample approach, which is valid for a content validity based selection instrument. As an example, the selection instrument asked an applicant to calculate monthly payments on a home given certain financial parameters. The questions were given to six randomly selected job incumbents who were asked to choose which of the job sample test questions an applicant would have to pass in order to meet minimum standards as a new employee. The job incumbents overall picked an average of 80% of the job sample items as being necessary for a new employee to pass to be acceptable at a minimum level of acceptability. Therefore, an applicant would have to score a minimum of 80% in order to be considered for employment.

As a check on the validity of the 80% cutoff score, the job sample questions were given to the four other job incumbents. All of these incumbents were considered to be satisfactory employees by the business owners, and all received a passing score of over 80%.

In summary, small business owners need to be aware of the UG, the court cases which have resulted from the UG, the one practical approach to validating a selection procedure, and the advantages to having a validated selection procedure. By following the outline of Robinson (1981) or the case presented in this paper, the small business owner can both enjoy the benefits of a validated selection procedure and lessen any worry over an EEOC lawsuit.

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EMPLOYEE TRAINING AND DEVELOPMENT FOR SMALL BUSINESS

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ABSTRACT

Small business owners/managers, concerned about costs, quality, and customer satisfaction, often overlook the role of employee training and development in these concerns. Employee performance problems are not always immediately obvious; thus, managers and employees working together can identify them. This requires problem solving and coaching skills in order to identify the performance problems (and their causes) and the skills or conditions required to resolve them and improve performance. By utilizing the same effective problem solving skills they use for other business problems, the small business owners/managers will be able to incorporate this vital element of their jobs into their daily operations.

INTRODUCTION

Today's business environment can be characterized as changing. The accelerated pace of advances in technology, increasing foreign competition, widespread and growing unemployment creating serious adjustment problems, and diminishing resource supplies have affected the way American business is conducted. This complex and unstable environment is a way of life which will continue far into the future. Small business owners/managers, concerned about costs, quality and customer satisfaction in this volatile environment often overlook the role of employee training and development in these concerns. This changing environment has focused attention on the need for quality performance-individual as well as organizational.

Quality performance requires that employees be capable, have clearly defined job roles, know what is expected of them, have the tools to do the job, have the knowledge and skills to perform, receive regular feedback on performance and understand and receive rewards for good performance. (5) These are the elements of an effective performance management system. In order to improve employee performance, management must clearly define and communicate the purpose of the organization - what is important to members of the organization in carrying out their work, organizational aims and goals, responsibility for achieving aims and goals and what constitutes successful accomplishment of the aims and goals - through an operational plan. (5) The performance management system and operational plan, clearly linked and supported by one another, are powerful means for focusing employees on attaining common goals and desired performance results.

Small business organizations, with their flatter organizational structures, are able to implement these two critical systems with more immediate results than larger organizations. Without the numbers of layers and gaps between management and employees, communication channels can be more open, making it possible for one level to listen to and learn from another. It is possible for new frameworks to evolve, facilitating working as teams for coordinated action that energizes learning among the group members. Utilizing these two systems there is a combination of different knowledge bases and viewpoints of all concerned with a single goal, project or product. This makes for mutual understanding and learning, brings management and employees closer together and achieves needed action. It also creates the possibility of reassignment of employees to different kinds of work which, while it may make individual roles less clear, does much to promote an attitude of continuous learning. This approach to the accomplishment of the work of the organization integrates employee training and development into the daily work environment by amplifying what is being learned through experience.

Peter Drucker has suggested that management people learn to ask "What do we do in this organization that helps you do the job you're being paid to do, and what do we do that hampers you?" (3) This question focuses on the ways managers enhance or inhibit the performance of their employees. Bradford and Cohen suggest that an entirely new definition of leadership is required, one in which shared responsibility and control takes the place of the individual hero carrying the burdens alone. (1) If all of the organizational members are committed to joint responsibility for overall excellence, the collective power and potential for excellence is marshalled through the commitment and abilities of the whole group. At the same time that the manager works to develop management responsibility in employees, he or she must help develop the employees' abilities to share management of the unit's performance. (1)

This increasing interest in participative management systems - quality circles; quality of work life, productivity and suggestion programs-requires an understanding of the need for a greater involvement of employees in problem solving, assuming greater responsibility for more activities and acting more independently. When managers view problems as developmental opportunities for employees' commitment and capabilities, they may turn problems back to employees for resolution, or ask questions to help them focus on key issues or work jointly with the employee. This approach not only resolves problems, but it helps the employee develop in a valuable training environment - the workplace.

Bradford and Cohen note that utilizing this manager as developer approach increases the chance that tasks will be accomplished at a high level of quality for task excellence is more likely when members seize new opportunities as they develop; uncover problems and difficulties early, before they become major crises; share their knowledge and expertise; and feel committed to carrying out decisions. (1)

A recent example of a participative management policy as a forbiddable weapon for overcoming problems is Herman Miller, Inc. of Zeeland, Michigan, an office furniture producer with a progressive management reputation. A slump in the computer industry, competition sparking discounting and manufacturing and delivery problems, all contributed to the first decline in 14 years. Rather than shift from participative management to manage by edict (which is quite typical), Max O. DePree, Chairman and Chief Executive said "That is exactly the time you ought to depend on it the most." Employees suggested cost cutting measures which saved $12 million and slashed delivery times through more effective production processes and sales developed significant business in weaker markets. Herman Miller tapped the full potential of its workforce, "employees have a real say about their jobs and get a fair share of the results ... when employee bonuses were falling, they were saying what can we do about the problems?" (6) The role of employee training and development is crucial to any effective and successful manager. Being able to get work done through the efforts of others is a key managerial skill which is often seen as a separate function which is performed by the individual charged with personnel responsibilities or considered a luxury item for busy small business owners/managers. one can become a more effective training and development professional when the process is incorporated into the daily management style of the owner/manager.

A universal rule of Japanese management is that job training is a supervisory responsibility - "it is the number one duty of the manager to develop, counsel and coach his employees." (3) A common rule in Japan, rare in America, is that production comes from the way managers manage. In this setting, managers are required to spend considerable time on personnel matters giving attention to the performance management system and the operational plan. These efforts contribute to a continuous learning environment in which the workplace is seen as a learning laboratory where learning and the improvement of work are integrated. (3) In such an environment, management and employees are working for the same goals, the success and prosperity of both the company and the individual worker, thus adhering to the key elements of individual and organizational quality performance.

How can the small business owner/manager take these broad, theoretical notions and apply them on an operational level? An important source of information about employee training and development needs is the employee's performance appraisal. The critical elements of an effective performance management system are planning and feedback appraisal. The planning process includes an assessment of the employee's capabilities, a discussion with the employee in order to clearly define job roles and expectations; identify the tools required to do the job; and to ascertain whether or not the employee has the knowledge and skills required to perform the job. This discussion can yield crucial information about performance discrepancies (the difference between actual and desired performance). The important point to remember here is that problems are being identified; solutions can only be developed after problems are identified. One common error at this point is for the manager to state "We've got a training problem." A performance discrepancy may have been identified, but the solution is not yet known.

Performance problems are not always immediately obvious; thus, managers and employees working together can identify them. This requires problem solving and coaching skills in order to identify the performance problems (and their causes) and the skills or conditions required to resolve them and improve performance. Problem solving and coaching are critical skills in the learning process. Coaches are helpers who effectively problem solve with the employee, calling upon their managerial problem solving skills. By utilizing the same skills they use to resolve other business problems, the small business owners/managers will be able to incorporate this vital element of their jobs into their daily operations.

Mager and Pipe suggest a performance analysis to find solutions to human performance problems. Beginning with a description of the performance discrepancy, one is asked to consider the following:

* Is it important? If no, ignore it. * Is it a skill deficiency? If yes: did the employee used to do it? is it used often? * Is there a simpler way? If yes: change job arrange on the job training * Does the employee have potential? If no: transfer or terminate * Is it a skill deficiency? If no: is performance punishing? is non-performance rewarding? does performance matter? are there obstacles to doing it? (4)

They note that following this problem solving approach will suggest solutions related to the problem without consideration of whether the solution is the most practical or feasible in the situation. They suggest a list of questions in order to compare the size of the remedy with the size of the discrepancy, including:

* Are there any solutions inappropriate or impossible to implement? * Are any solutions plainly beyond our resources? * What would it "cost" to go ahead with the solution? * What would be the added "value" if I did? * Is it worth doing? * Which remedy is likely to give us the most result for the least effort? * Which are we best equipped to try? * Which remedy interests us most? (Or, on the other side of the coin, which remedy is most visible to those who must be pleased? (4)

This problem solving model provides a practical, realistic approach to analyzing employee performance problems for it focuses on problems and their causes before attention is directed to potential remedies.

Feedback, another critical element of effective performance management, requires that managers give employees specific, accurate information about performance. One of the most effective ways to do this is through critical incidents and a file system. By keeping an informal file on each employee, a manager can record notes concerning performance events and the resultant discussion with the employee. For example, on July 15, 1986, Chris submitted the report with all the quarterly finance data. The report was complete, required no corrections and was forwarded to the President's office (discussed with Chris on July 18, 1986). Or, on July 15, 1986 Chris submitted the July 10, 1986 report without production data. Additional information required held up the report from filing until July 18, 1986 (discussed with Chris on July 10, July 15 and July 18). These critical incident reports help managers and employees understand job standards and expectations, work collaboratively to maintain or improve performance on an on- going basis and provide realistic, balanced information for the formal performance appraisal interview.

Employee development in an effective performance management system focuses on areas which require changes in order to improve performance. Performance appraisal is used to analyze progress and identify problem areas, providing feedback to correct the performance discrepancy instead of punish substandard performance and to suggest needed adjustments. Thus employee development allows the education and training function as a part of a broad performance improvement effort with critical support from management. (2)

Employee training and development is an on-going process; people learn at the workplace everyday. Small business owners/managers can maximize this learning opportunity by building an environment of greater trust and commitment in the workplace through respect and involvement of employees. By linking successful achievement to personal and organizational goals, the performance management system focuses employees on attaining common goals and desired performance results.

Utilizing the workplace as a learning environment enhances a manager's role as a more effective manager, thus making employee training and development a critical responsibility of each managerial job. Facilitating the learning of others requires different roles. The formal role of teacher is often too time consuming and threatening to managers who are concerned about being at the podium or "getting the work out." Informal resources-supervisors/managers, advice, counsel, networks, work teams, audio-visual-are often overlooked or inadequately utilized.

The workplace is a learning arena. Effective owners/managers function in different ways to help people learn. Experiential learning techniques and self-planned learning are two models which can be utilized in the workplace. Peer teaching, mentoring, coaching, small group discussion, job rotation, workplace rearrangements, meetings and work team participation are other potential learning resources. Each one of these alternatives can be used individually or in conjunction with other methods. But they are all readily accessible to the individual manager.

It should also be recognized that each one of these alternatives requires that the small business owner/manager share information and involve the employee in the total process. This does not mean that the manager must relinquish power, but that it must be shared-necessary responsibility, authority and accountability required to get the job done. This is difficult for many small business owners/managers, for they began by doing it all themselves. They were able to progress to their present level by maintaining many responsibilities. But this has to change if they are going to continue to grow and succeed. Flexibility is a requirement of the job. Thus, effective employee training and development is not "just a nice thing to do" but a necessity for continued business success.

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FRANCHISING ORGANIZATIONS: USING STRATEGIC PLANNING

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ABSTRACT

Historically, organizations have relied primarily on financial forecasts for their planning and organizational development. However, a major shift is taking place in franchise organizations. Strategic planning and strategic vision are moving franchises forward into the 21st century. The franchisor today utilizes the strategic planning method as a key element of the franchise organization.

INTRODUCTION

Traditionally, franchising organizations have lived by the gut feel and inspiration of the founder/owners. Today, that "feel" is bringing franchising organizations out of the darkness into one of the widest utilizations of strategy planning in business.

The system is radically different from most strategic planning models and develops some useful tools in the strategic management process. "To plan or not to plan is not the question." This no longer is the franchising dilemma. Rather, after developing strategy, how do you organize to achieve the mission of the organization in a growth environment?

It is important to understand the difference in organizational structure between a franchised and non-franchised business. In the non-franchised business, the typical organization chart has the president or CEO at its apex with the various vice presidents occupying the next level and so on down the line. Many franchised organizations are structured quite differently because of their special way of doing business. Typically, their organizational chart is an overlapping of Administration, Sales (that is, acquiring new franchisees), and Operations (working with the franchisee once "on board").

Not only must the franchisor understand that their organization is structured differently, but they must also recognize that a basic underlying assumption of the strategic planning process in the franchising system is that they are going into business in a changing environment. With this in mind, the franchising strategic management process can be broken down into four major components: (1) the strategic vision, (2) specific strategic process, (3) the implementation, and (4) the stewardship of the program by the franchisees and lower managers. When properly completed, these four factors develop one of the most unique strategic planning methods available in business.

STRATEGIC VISION

A process often unique to the franchise organization is the development of a strategic vision - an ability to articulate the mission, goals and direction of the organization. This is primarily a communications step wherein the owner pictures for the other members of the organization and the franchisees the actual place of the organization in the economy and in society.

The secret of the strategic vision as Jim Peterson (President, Whataburger, Inc.) stipulates: "is to be able to communicate this vision to those who are working with you and for you. This vision cannot be put down on paper, but rather is an accurate picture and portrayal of the organization in its environment."

STRATEGIC PLANNING PROCESS

Strategic planning processes vary from one organization to another. No two are identical. However, there are some unique factors involved in strategic planning for a franchise organization that may or may not be applicable to a non-franchising business.

The first step in most strategic managing processes is concerned with the development of the mission statement and its relevance to the business. Franchising requires that, during the development of the mission statement, the basic business assumptions required for the business also be developed and that the objectives of the business be prioritized.

The mission statement of a franchise basically explains what the owner wants to be or to become, and the objectives stipulate what the owner wants to have. These objectives, because of limited resources present in all franchising organizations, require a prioritization, generally on a one-to five-year basis. Assumptions are of vital importance to the franchising operation. These assumptions are from both the macro-and the micro-fields and require a close scrutiny of operations to make sure that a franchisee in a specific location may actually be a success in that location. For example, the franchisor must assume an available cash flow on the part of the franchisee, that the franchisee will honor the contract and maintain the quality standards of the parent franchisor, and that the franchisee will adequately prepare and deliver the product to the consumer in an efficient and proper manner. In short, the franchisor must assume that any new franchisee will essentially meet or exceed all "requirements" for being successful/profitable.

Many franchise organizations never do develop the mission statement or prioritize their objectives before launching into one of the most vicious growth-oriented operations available in the American economic system.

Strategic plans are designed to explain "how to achieve wants". The actual plans are those detailed programs supporting the strategy of the business. Included in those plans are annual budgets which are developed around the mission and objectives of the organization plus marketing and organization/manpower plans. During the planning process, everyone is involved in the budgetary plans. These are developed for all units and organizations within the franchise.

The organization plan is also concerned with the manning process and is very important to the franchising organization. If the organization is going to grow in units and in numbers, then the headquarters operation is also going to have to increase their staff and delivery capability. A major question concerns where the people are coming from: (1) internal staff members, (2) franchisees, (3) external sources.

Marketing plans, however, are handled much differently. Unlike most organizations, franchisors develop two marketing plans. One plan is targeted to the ultimate consumer and, so, is parallel to that of most any organization. After its final completion, it is passed through the entire organization including the franchisees. The second marketing plan is targeted to developing and acquiring additional franchisees and, so, is kept secret and separate by most franchisors.

This strategic planning process develops a total management philosophy and requires much more than cursory involvement by the CEO. This process also requires the development of a proper environmental analysis including the external as well as the internal functions.

IMPLEMENTATION

Franchising, unlike many corporate organizations, requires a continuous implementation of the strategic management process. This implementation from the franchisor to the franchisee requires constant supervision and development at the franchisee level. With new franchisees constantly beginning their businesses, the franchisor is continuously striving to develop and implement the business plans and franchise format within that unique, separate business.

The implementation of a franchisor's strategic management plan includes the traditional corporate levels of executive, division and departmental. However, franchising also presents the unique problem of introducing the plan into a business owned and operated by somebody entirely different and "independent". The franchisee is one of the main recipients of the franchisor's strategic plan. The implementation, therefore, of the plan by the franchisor requires an extensive selling or marketing program on the part of the franchisor. Bob Rosenberg recently announced that 94% of the Dunkin' Donuts franchisees voluntarily raised their advertising fee from 2 to 4% of gross sales annually because of the strategic plan shown to them. This new plan from Dunkin' Donuts required extensive marketing and advertising costs in excess of current revenues. The franchisees, after analyzing and reviewing the strategic plan, voluntarily adopted it for their own franchised outlets and are now contributing a 100% increase in their advertising budgets to the franchisor.

STEWARDSHIP BY FRANCHISEES AND/OR MANAGERS

A unique aspect of the franchising strategic plan is that the main implementation is done by people outside of the business itself. The franchisor's strategic management plan is actually stewarded and overseen by the franchisees, not the franchisor.

These plans often involve close review and inspection. The measurements sent by the franchisee to the franchisor often include financial data and are presented on a weekly (sales, cost of goods sold, and labor costs) and monthly (revenues and expenses) basis.

The franchisee also develops reports to be presented at monthly or quarterly meetings describing their progress against the objectives or goals of the organization. Additionally, activity reports are sent in periodically to the franchisor regarding different projects which the franchisee may be developing.

So, in practice, the strategic management process is from the bottom up rather than the top down in most franchising organizations. It is of primary importance that the franchisee adequately understand and implement the plan of the franchisor.

Incentives

Most franchisors have discovered the need to reward performance. This performance is based upon the achievement of the strategic plan and allows franchisors to properly award and provide incentives for franchisees to excel. The franchisees may receive plaques, honors, travel trips, resort vacations, electronic or video appliances or even cash. The departmental or branch managers may receive a commission on a monthly, semi-annual or annual basis. The department heads may receive incentives of annual bonuses with 50% of the draw available each six months. The corporate officers may receive an annual bonus of "x" percent up to 20% ROI, or 2 times "x" percent over 20-25% ROI or 4 times "x" percent over 26% ROI. This encourages all levels of the organization to maximize the efforts and to improve the productivity of the franchising organization.

SUMMARY

Strategic management is very important to the franchisor. This planning tool is becoming very important in modern day franchise activities. Franchisors have realized the need to develop a strategic vision or picture of the business and to be able to explain the vision or picture to others interested in the business. In addition, the franchising process requires careful planning based upon certain assumptions and the priorities of objectives. The implementation is continuous and the planned success is the responsibility of people external to the headquarters organization -- the franchisee.

DEREGULATION OF WORKERS' COMPENSATION BENEFICIAL TO SMALL BUSINESS?

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ABSTRACT

One of the most significant regulatory trends affecting small businesses is the deregulation of workers' compensation insurance. As the states debate the merits of various aspects of workers' compensation insurance reform, it is important that the small business community understand the relevant issues. This paper explains these issues and how this changing regulatory environment will affect small businesses.

INTRODUCTION

The substantial increase in industrial injuries during the 1960s gave rise to the Occupational Safety and Health Act of 1970 (administered by OSHA) and a broad wave of reform in the states' workers' compensation laws. Workers' compensation laws, which make employers responsible for medical costs and lost wages associated with on-the-job injuries and diseases, were changed in a relatively straightforward manner during the 1970s. Benefit levels were substantially increased and coverage broadened to include virtually all employees. While these reforms were somewhat controversial, there was a consensus as to the appropriate direction of change. Inevitably, as a result of these changes in coverage and benefit levels as well as increased filing rates, the costs of the insurance required to meet these obligations rose significantly. In the period from 1972 (the year the National Commission on State Workmen's Compensation Laws issued its guidelines for reform) through 1978 (the peak year), the cost of workers' compensation as a percentage of payroll increased over 80 percent.

In response to these cost increases. the states are engaged in a second wage of reform aimed at some of the more subtle features of the system. The cost containment issues being debated in the 1980s include eligibility for permanent partial benefits, desirable administrative arrangements, and pricing regulation. It is the purpose of this paper to consider the issues of pricing regulation and to describe their implications for the small business community. Recent surveys of small businesses indicate workers' compensation insurance costs and the impact of deregulation on these costs are of great concern. The paper begins with a brief description of premium setting in the traditional administered pricing states. A parallel discussion of the legal environment in states that have adopted competitive rating laws is then presented. The specific issues of regulation relevant to small business are then discussed--these include the impact of open competition on general price levels, the role of expense constants in administered pricing. the use of group self-insurance, and the role of experience-rating. A concluding section addresses whether, on net, deregulation is favorable to the small business community.(l)

ADMINISTERED PRICING

Workers compensation insurance is provided in a variety of ways. The most common mechanism is coverage supplied by a for-profit insurance company. In most states larger organizations are allowed to self-insure their liability subject to state approval. Several states run their own workers' compensation insurance fund in competition with commercial insurers. while six states have monopoly funds that do not allow private competition.

Premium levels, even for the commercial insurers, have historically been set by the state based on information supplied by a state-level rating bureau sponsored by the insurance industry. The loss experience of up to 600 industrial/occupational classes is considered and the rating bureaus recommend a set of "manual rates." The state then approves a premium structure based on this information. Once the manual rates are set by this governmental process, insurance companies place their customers into the appropriate classes and the total manual premium (manual rate times payroll) is then determined. If a business is large enough, its manual premium is adjusted in consideration of the firm's experience. A formula set by the state is used for this experience- rating. In those states with a governmental insurance fund a similar process is used to administer the price a charged for insurance. Self insurers may, of course, "charge" any price as long as they meet the liquidity requirements set by the state.

Hearings over the workers' compensation rate levels are much the same as administered price debates in other contexts. Various interest groups make their cases with the help of a variety of expert witnesses testifying as to the appropriateness of various rate structures. As usually practiced, this system led and in many states continues to lead to a rigid system in which prices are isolated from market place pressures. The impact on price level of these restraints will be addressed below but the broad conclusion must be that prices are usually higher than they would be under more direct market competition.

OPEN COMPETITION

During the late 1970s and early 1980s there was a wave of price deregulation in many significant American industries. Airlines, railroads, bus companies, financial institutions and many others are still adjusting to this radical change. While many forms of property and liability insurance have historically been price regulated, almost half are now priced through the direct influence of market forces. The only major exception is workers' competition insurance which still uses administered pricing in all but ten states (Arkansas, Georgia, Illinois, Kentucky, Maine, Michigan, Minnesota, Oregon, Rhode Island, and Vermont). The characteristics of open competition vary among these states. In general the insurance bureau still plays a role in developing pure premiums, that is premiums that do not include profit or non-claim expenses. Knowing the combined loss experience of each of the industry/occupational classifications across all insurers is quite valuable for insurance companies in pricing their services. This information is still available under open competition.

While only ten states have adopted open competition laws, strong elements of direct market forces are being felt in most administered pricing states. Devices such as retrospective rating, extra discounts on non-regulated lines of insurance, and special credits for particular characteristics of an employer such as safety programs are used to adjust the administered price to a level more compatible with the dictates of the marketplace. Unfortunately such devices tend to be much more widely used with large employers--small businesses are frequently locked into the administered price.

RATING LAW IMPLICATIONS

There are five key areas in which administered pricing and open competition influence small businesses and their workers compensation insurance. These areas are the impact of competition on the overall price of workers' compensation insurance, the use of expense constants under administered prices, the use of assigned risk pools, the legality of group self-insurance, and the role of experience-rating.

Competitive Rating and Prices

Insurance companies usually claim that the mechanisms of administered pricing serve to keep premiums below those needed to maintain appropriate and adequate profit levels. On the other hand, experience in other administered pricing situations indicates that competitive prices are usually significantly below those set by governmental processes. Surely it is the case that in some states administered prices are below competitive levels and in some states they are above the competitive level. In the states that have introduced open competition in the 1980s, the tendency have been for prices to fall significantly. However, the period of this deregulation has been one of historically high real interest rates and this may bias the true pattern. When interest rates are high, an insurance company is particularly interested in collecting premium dollars in order to earn profits on investments. They are willing to cut premiums even if they are not high enough to cover all eventual losses. This phenomenon is particularly important in workers' compensation where loss pay-outs are often phased over decades.

When Michigan deregulated workers' compensation insurance prices in 1983, a well- documented analysis found a 30 percent decrease in premium levels. This significant decrease in prices does not necessarily represent what would happen in other administered price states and, as stated, it may be partly due to the coincident high interest rates. However conditioned the conclusion, it is clear that open competition will usually result in lower average premium levels for the overall market.

Expense constants

While it is fairly clear that average prices will usually fall (or not go up as quickly as they otherwise would) under open competition, it is not clear how this change in prices will affect large versus small firms. It is apparent that there is often an advantage to small firms built into the administered prices. When the price structure is set by state government, a constant dollar amount for expenses is allocated to each policy. (There are other ways in which administrative expenses are built into premium levels but they are not of direct relevance here.) This "expense constant" is charged to all policies regardless of size. The permitted level of this factor (averaging about $100) is trivial for firms of moderate or large size but can be quite significant for small businesses.

The fixed costs of writing workers compensation insurance policies typically appear to be above the mandated level of this constant. This is not significant for larger businesses but in many cases it does provide an advantage for small businesses. Small business organizations apparently recognize this and frequently lobby during the rate-making process to hold down the expense constant. Under open competition, each insurer can set its own expense constant and therefore it would surely tend to raise in this environment.

Assigned Risk Pools

Workers' compensation laws mandate that all firms obtain insurance to cover their potential liabilities. Therefore, if a firm cannot obtain voluntary insurance, they are placed in an "assigned risk pool." This pool is operated by several of the commercial insurers with the expenses shared by all insurers operating within the state. In many states small businesses are relegated to this assigned risk pool--most likely because the premiums they would generate do not adequately reward the insurance company for covering their potential losses. This then is evidence that with the more flexible pricing of open competition, premium levels for many small businesses would increase. (2)

Group Self-Insurance

If a firm believes that insurance industry prices are too high it can usually consider self- insurance. However, because the pooling of risks over a large number of potential losses is a key part of insurance, this option is generally available only to large employers. In several states, however, groups of small firms have combined to form insurance pools that have many of the advantages of self-insurance. This device is obviously of significance only in those environments where regulated prices have caused premiums to rise above what is justified by potential losses. Individual self-insurance is a quite popular technique for avoiding high premiums in such situations. The states that allow groups of small businesses to join together for self-insurance have also had quite a successful experience. Unfortunately many states do not allow group self-insurance by small businesses.

Experience-Rating

A final dimension of the regulatory environment that is important to small businesses is that of experience-rating. The loss experience of a small business over a one, two, or three year period is not abroad enough base of experience for actuarial purposes. As a consequence, small businesses pay premium rates that are strictly a function of the industry/occupational classification rather than their individual experience. Many small businesses have excellent safety records, yet they are paying premiums that reflect their classification's average losses. Is there a way to relate premiums and losses that would be fairer for the small business? There can be no definitive answer to this question; however, it is clear that the governmentally determined pricing arrangements have discouraged experimentation with alternative forms of experience- rating. In the administered price states, the experience rating formula that precludes participation by small businesses is mandated as a part of the regulation. Clearly open competition will be more receptive to this experimentation, but whether it will yield any significant changes has yet to be determined.

SHOULD SMALL BUSINESS FAVOR DEREGULATION?

As noted in this review of the issues, the regulatory environment of workers' compensation strongly influences the impact of this program on small businesses. The typical downward bias in expense constants has created an image of significant advantages to administered prices in the minds of many small business advocates. Within the context of administered prices, small businesses do receive some advantages relative to their larger counterparts. However, the broad price reductions of deregulation and in particular the flexibility of arrangements for self- insurance and experience-rating associated with the openly competitive environments make it likely that small businesses would be better off with this new method of structuring the insurance market. Furthermore, in those states that continue with administered prices, it is clear that flexibility can be introduced to serve the small business community. Experimentation with group self-insurance, scheduled rating credits and new experience-rating methods are all options with in the administered pricing system that should be explored and encouraged.

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PERFORMANCE MANAGEMENT IN THE SMALL ENTERPRISE

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ABSTRACT

Human resource managers are coming to realize that distinct practices must be developed for the small organization. This paper describes the characteristics of the small organization which require a different approach to performance management. A performance management system which meets the needs of the small business, the employee of the small business, and the requirements of Fair Employment Practice legislation is discussed.

PERFORMANCE MANAGEMENT

Performance management techniques in use in larger organizations do not transfer well to the smaller enterprise. A large organization will devote time, energy, and capital to define performance for individual jobs, develop measures of performance, establish goal setting programs, train managers in the use of appraisal techniques, and create formal systems to administer appraisals and link other human resource processes such as promotion, discipline, and compensation programs to appraisal outcomes. (l) Smaller organizations rarely have the resources to devote to the development of traditional performance management programs, and the culture of informality present in many small businesses would not support such programs in any case. Even if there are resources and a supportive culture the small numbers of individuals in similar positions in the typical smaller organization makes the development of traditional programs cost inefficient. Perhaps the most important reason for the inapplicability of traditional performance management programs in small business settings is the nature of the job/worker relationship.

In the larger organization jobs are designed to support the organization in meeting its overall goals, and workers are then selected who best fit job specifications in terms of their knowledge. skills, and abilities. Job performance is defined independently of the employee hired to fill the job. (2) In the smaller organization this process is frequently reversed; that is, jobs are frequently designed around available employees. In family owned enterprises, for example, jobs may be created for individual relatives and job descriptions are tailored to fit the individual employees' knowledge, skills, and abilities and his or her preferences. In smaller businesses one employee may handle a variety of tasks each of which in a larger organization would constitute a job. The way in which these tasks/jobs are allocated across workers is a function of the workers available to the organization and the decision is frequently made after one or more workers is hired. These allocations are also less stable in the smaller business than in the larger business; the turnover of a single employee in the small business may result in a complete restructuring of a large percentage of the jobs in the organization, depending on the knowledge, skills, and abilities of the replacement.

Even though traditional performance management programs are unlikely to work in small organizations, these organizations have perhaps a greater need for successful performance management programs than large ones. This is because small organizations have less slack than large ones and are less able to withstand the effects of poor performance. The poor performance of a single worker has proportionately greater effect on the small business. In addition, most small businesses (all those with more than 15 employees) are subject to Federal Fair Employment Practices legislation (3) and in some states all employers, regardless of size, are subject to state FEP legislation. The best justification for most human resource decisions (e.g., firing, non- promotion) challenged by a disgruntled employee is documentation of poor performance coupled with documentation of performance management practices. (4)

How then, should the small business manager approach the performance management problem? In fact, while the beginnings of the performance management process are similar for large and small organizations the issues are perhaps easier in the small organization. This is because the starting point, specifying the goals of the organization, probably deals with a less complex goal set in the small organization, and because the small business manager is likely to be familiar with most aspects of the operations of the organization.

As a first step, the manager must specify the goals of the organization. (5) If the manager is not in charge of the entire organization then the goals specified should be those of the unit in which he or she is in charge. The unit goals must, obviously, be supportive of the larger organizational goals, developed using the cascading goal principle. (6) These goals should be stated in fairly specific terms, in list form. Sample goals might be number of units produced, units of service provided, cost per unit, new customers attracted, or turnaround times. In the larger organization these goal sets are related to the task sets, or jobs, which are required to accomplish them.

In the small organization these goal sets can be more effectively linked to the employee sets, or work groups, which are required to accomplish them. Thus, for the goal "produce 400 units of product 'x'" the manager might designate 10 employees to constitute a goal achievement team (GAT) responsible for accomplishing that goal. Most workers will be associated with more than one goal achievement team since several goals may be related (e.g., production, cost savings, safety, lowered customer complaints). It is important that artificial boundaries not be set for GATS nor that the number of goal achievement teams to which an employee belongs be unduly restricted.

The manager may take two approaches toward establishing goal achievement teams. Employees may be assigned to specific GATS by the manager on the basis of past performance, needs of the organization, and skills, or employees may choose their own GATS. Some middle ground serving-both the needs of the organization and the wishes of the employee is preferable; one reward option open to the manager is allowing employees to bid on GAT assignment with past performance scores being the basis for determining winning bids. However, as with most forms of employee participation it is important that it be clearly communicated by the manager that any decision reached is subject to approval by management. (7) It is equally important that this approval be withheld only in extreme cases.

When a goal achievement team is completed, the manager meets with the members and describes the goal and activities required in achieving the goal. It is in this meeting that performance standards for these activities are defined by the manager and communicated to the entire team. If the goal requires complex activities requiring specialized work assignments those assignments can be made in this meeting. Some degree of participation should be fostered by the manager, and the team itself may decide on work assignments within the team. Management performance standards for individual work assignments can be communicated at this meeting. Group discussion should be held to make sure that all members understand what the performance standards are, and what responsibilities of individual team members are. This use of team-building technology will maximize group and individual commitment to the group goal. (8)

Managers must be careful to make sure that both behavioral and outcome performance standards are covered in these meetings. (9) One of the problems in many goalsetting programs in organizations (such as MBO) is the exclusive use of outcomes as goals. (10) If outcomes alone are used as goals management may find subordinates working to meet specific outcome goals neglecting quality and long range requirements such as maintenance and safety activities. Equally poor results may occur if behaviors alone are used as goals, since employees may go through the behavioral motions required but show little concern for concrete outcomes. (11) Successful goal setting programs emphasize both what outcomes are desired and what behaviors are desirable in attaining those outcomes.

When all goal achievement teams have met the manager needs to aggregate the various goals/work assignments/ performance standards for each employee. In most cases this will simply be a copy of the set for each GAT to which the employee belongs. These goals/assignments/standards form the performance contract with the employee and the manager should make sure that everyone considers it as such. This view can be enhanced in a meeting between the manager and the individual employee in which the performance contract is briefly discussed and signed by the employee.

It is when a new employee joins the organization that the difference between the GAT approach and the traditional job standards approach becomes most evident. In the traditional job standards approach, a job opening occurs due to expansion or turnover. The vacant job has standards attached to it which are independent of any incumbent. The manager seeks to fill the job with the applicant thought likely to perform the best against those standards.

In the GAT approach one or more goal areas requires an additional employee if the organization is to achieve its goal (s). The manager, when interviewing applicants, looks not for someone to fill specific job requirements, but instead matches applicant knowledge, skills, and abilities against the entire set of goal achievement requirements. This gives the manager much more flexibility in the hiring process. The goal achievement team can be made part of the selection process, providing both a realistic job preview to applicants and providing additional selection decision information to the manager. (Peer selections tend to predict future performance much more reliably and validly than superior selection decisions.) (12)

When the employee first starts work the manager should sit down with the new employee and discuss the performance management and GAT concepts. The specific goals, tasks associated with those goals, and performance standards need to be communicated to the employee. (13) As noted above, these goals/tasks/standards form the performance contract with the employee, and it should be explained at the beginning of the performance period precisely how the manager will rate different performance levels. While the manager may wish to have the employee participate in determining which GATS and tasks the employee will be assigned to, the performance standards are managerial prerogative, and stem from an organizational imperative. When it is clear from the discussion that the new employee understands what is expected of him/her, the performance contract should be signed and a copy given to the employee.

At this meeting the consequences of various performance levels should be communicated to the employee. If there is a merit pay system of any type based on performance outcomes the typical increases or increase differentials based on performance differentials should be communicated. While managers must be careful not to make specific promises ("You perform at the '5' level and you will get a 6% raise.") they are not sure they can keep it is unrealistic to expect any system to motivate high performance if the employee has no perception of links between performance outcomes and other valued outcomes such as salary increases, promotions, or task assignments. (14)

During the performance period the manager will provide positive feedback to the employee when the employee is performing above standard. Many managers make the mistake of giving employees negative feedback only. on the principle of management by exception. The literature indicates that this is the least effective means of motivation available to managers. (15) Positive feedback is a strong motivating influence. and serves to increase job satisfaction as well.

While providing positive feedback, the manager must provide coaching. That is, when the manager observes an employee behaving incorrectly, or performing below standard, the manager coaches the employee to improve performance. (16) While negative feedback is included in coaching. the manager makes judgements not about the employee as a person, but about the behavior/performance of the employee and treats the incident as an opportunity to help the employee solve a problem rather than punish the employee for an infraction. When the employee is able to correct the performance deficiency the manager provides immediate positive feedback.

The goal achievement team members can provide positive feedback and coaching to team members and should be utilized for these tasks. The management literature provides ample documentation of work group constraints on individual performance. (17) The work group motivated to high levels of group performance by the GAT process will induce high performance levels from all its members. Indeed, quality circles and other limited purpose work groups have demonstrated the effectiveness of this approach. If the GAT is to be formally utilized in coaching/feedback activities, some training should be provided to it by the manager in these activities. (18)

During the performance cycle. the manager should keep an informal performance diary on each employee. (19) This is because most people have faulty and incomplete recall of past events. When the formal appraisal is made at the end of the performance cycle, most managers will be unable to provide concrete examples of performance from other than the last month or two of the cycle. In this diary, the manager simply jots down during the cycle specific incidents which at the time typify the employee's performance. The diary serves as documentation for any performance related decisions which may be made.

At the end of the performance cycle, the manager will set up an appointment with each employee for a performance appraisal interview. While the employee has had fairly continuous feedback, a summing up is useful. The manager should aim for a "no surprises" appraisal interview. To this end, the manager should provide the employee a completed copy of the appraisal form prior to the interview, so the employee has time to digest the manager's summary and can prepare an alternates for discussion.

The precise format used for the appraisal is not crucial. The form should contain the key outcome/behaviors designated at the beginning of the performance cycle as the performance contract. The manager's summation of employee performance with respect to each outcome/behavior should be noted. Incidents from throughout the performance period illustrating performance should be referenced. (These come from the diary.) (20)

The manager may wish to get other members of each goal achievement team with which the employee is connected to provide input for the performance review. Peers usually observe performance of a team member more carefully than the manager, and may provide more reliable information than is otherwise available to the manager. (21)

In the appraisal interview itself the manager will do three things. First, the manager will discuss the performance summary with the employee and allow for employee input and correction (if warranted). Second, the manager will concentrate on one or two areas for improvement, and work out a plan for improvement with the employee. This planning will include reminding the employee of performance standards for the area needing improvement, goal setting activities for the coming performance cycle, discussion of means of reaching the goals (including activities required on the part of the manager), and specific dates to serve as checkpoints for progress. (22)

Discussion of the consequences of the performance level achieved by the employee is the third major component of the appraisal interview. Some possible consequences include pay changes, GAT assignment changes and changes in probation/ disciplinary status. If the manager does not have specific information on these consequences, some estimates or probabilities can be communicated to the employee. Some researchers argue that discussion of consequences and developmental aspects of the appraisal interview must be separate, since employees will concentrate on the outcomes and not pay sufficient attention to developmental aspects of the interview. (23) Precisely the same logic indicates that consequences should be discussed, since until consequences are settled in the mind of the employee little attention will be paid to development.

If the goal achievement team is closeknit and the culture of the organization supports the practice the appraisal interview can include the GAT and speak to the performance of all GAT members. However, such practice would require very high trust levels among team members and some experience with team-building and other organizational development technologies.

Many small business managers are not prepared to manage performance in the manner described. Yet many of these managers carry out many of the parts of the performance management system already. The typical small business is run informally and the manager has one-on-one dealings with most employees. Performance is observed by managers on a regular basis. Typically, employees of the small organization already participate in many task decisions and take responsibility for determining how things are to be done. In organizations in which these operating characteristics are the norm the implementation of the performance management process and the GAT approach require training which will allow managers to integrate much of what is already done. In less well-developed organizations more training will be needed. In either case. implementation can be made using a piecemeal approach.

Documentation required for the purposes of making and justifying human resource decisions flows naturally from the process described. The performance contract describing goals, tasks and activities, and performance standards are created at the beginning of every performance cycle. Specific incidents illustrating performance are noted by the manager in the performance diary during the performance cycle. To the extent that the goal achievement team plays a role in performance documentation that information is available. The summary of performance prepared for the appraisal interview documents the manager's integration of all performance data, and the performance plan developed in the appraisal interview documents remedies to which the manager and employee have agreed. Again, if the GAT provides input to the process additional documentation is available. All of this information, with employee reaction, placed in the employee's permanent file, provides adequate documentation to counter unjustified FEP claims made by disgruntled employees. (24) More importantly, following the performance .management process described. especially if full use is made of the goal achievement team approach, will result in employees performing at higher levels.

Some aspects of performance management programs typical of larger organizations are down- played or omitted in the program described. These include detailed job analysis schemes, emphasis on appraisal format development, and extensive training of managers in appraisal skills.

Job analysis efforts generally form the base of most human resource management programs. (25) In the small business elaborate programs are neither economically feasible nor are they necessary. The performance management system described is employee based rather than job based because in the small business there are frequently many tasks which must be done but do not require the full time of a single employee for their accomplishment. As a result tasks may justifiably be clustered around a specific employee based on that employee's particular knowledge, skills and abilities. Further, such clusters may justifiably be adjusted to take into account changing knowledge, skills, and abilities of the employee stock available to the employee. Changes in manager's needs increase the justifiability of orienting clusters towards specific employees. In short, employees may be more constant for the small organization than jobs; given the informality and the importance of personal relationships characteristic of the small business it makes more sense to build performance goals and standards around employees rather than jobs. Adequate job information is generated in the performance management process to serve the needs of the organization.

Appraisal format efforts can be minimal in the small organization using the performance management process described. Format development has an extensive literature, as does likelihood of rating error by managers using different formats. (26) Most format development is related to specific jobs and requires large numbers of job incumbents and/or other job- knowledgeable individuals for useful formats. Both requirements make format development impossible in most small organizations. Even when appropriate formats are developed in the larger organization there is little guarantee of reliable or valid ratings, although extensive training of raters can increase reliability and validity. Most researchers, even when dealing with larger organizations, have begun to focus on the entire process of appraisal and performance management, much as described in this paper. The gains evident from extensive investment in format development and training of managers simply to do a better job of filling in rating forms do not seem to be large enough to justify the expense.

This paper describes a performance management system developed for the small business which should meet Fair Employment Practice guidelines and which, more importantly, will help the management of the small business improve the individual and collective performance of employees. The system described takes the employee as the unit of analysis rather than the job, and concentrates on the personal, informal approach typical of most small businesses.

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PERSONNEL PRACTICES OF THE NATION'S SMALL BUSINESS OWNERS/MANAGERS

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ABSTRACT

Personnel problems in employing, training, and retaining quality employees in small businesses are becoming severe. This paper employs a national sample of small business owners/managers in studying various employment practices and perceptions of the small business owner or manager. A number of hypotheses concerning employment practices of small business owners/managers were tested at the 95% level of confidence. A prior assumption of small business difficulties in finding and retaining employees was supported. Reasons that employees leave a business are different for full and part-time employees. Thus, further research on the subject of small business employee retention should examine full-time employees and part-time employees' motivation separately.

INTRODUCTION

At one of the recent state White House Conferences, some business persons were concerned with the recruitment, training and retaining of quality employees for their small businesses. It was their opinion that many of their current employees were of low quality, and they appeared to be concerned over how to recruit and retain higher-quality people.

It appears to be common knowledge that personnel problems in employment and retaining quality employees in small businesses are becoming severe. In fact, this problem is becoming so severe that the Small Business Administration has issued a request for a proposal to study employment problems in small business.

According to this request, the percentage of the labor force aged 16-24 years has been declining. Because small firms supply 2/3 of entry-level workers with jobs, this implies an increase of wage levels for entry-level workers because of diminishing supply. It might also imply a declining unemployment rate for entry-level workers.

McEvoy [1] states that surveys investigating reasons for small business failures have often placed personnel-related problems at or near the top of the list. Solomon [2] states that no business can afford to hire inadequate personnel. The small business is particularly burdened in this respect since each employee constitutes a large percentage of the work force.

PURPOSE

The purpose of this study is to determine if there are significant differences between types of businesses and various employment practices and perception of the small business owner or manager.

HYPOTHESES

In this study, the following hypotheses were tested at the 95% confidence level:

H(1) There are no significant differences between types of business and the sources of finding employees.

H(2) There are no significant differences when one compares the sources of finding employees and the length of time the business has been in operation.

H(3) There are no significant differences between the type of business and reasons employees leave the firm.

H(4) There are no significant differences when one compares the reasons employees leave firms and whether the employees were employed full or part time.

H(5) There are no significant differences between the type of business and length of time the business has been in operation and the employer's perception of the greatest strength of new employees.

H(6) There are no significant differences between the type of business and the employer's perception of the greatest weakness of new employees.

H(7) There are no significant differences when one compares the type of business and the employer's perception of whether employees use their small business experience as a "stepping stone" to obtain employment in larger companies.

METHODOLOGY

The information included in this study was gathered, by using a questionnaire, from small business owners or managers throughout the nation. A list of Chambers of Commerce in the United States was obtained, and 48 Chambers were selected. A letter was sent to each of the 48 Chambers selected requesting a list of their membership.

Twenty Chambers (41.7%) responded by sending a complete list of their memberships. A weighted random sample, based upon population of geographic areas that the Chambers represented, were selected from each of the 20 lists.

A questionnaire was developed that requested information on 26 different items. This questionnaire was mailed to 223 small business owners on May 30, 1986; 258 small business owners on June 13, 1986; and 327 small business owners on June 30, 1986, for a total of 808. Each of the three mailings requested that the respondents complete and return the questionnaire within a thirty-day period. A final cut-off date, for the return of the questionnaires, of August 15, 1986, was used. Questionnaires returned after August 15, 1986, were not included in the study. By August 15, 1986, 236 questionnaires were returned, for a 29.2% return. The respondents were from 17 of the fifty states.

FINDINGS

Of those businesses reporting, 48.3% were retail; 28.7%, service; 7.4% wholesale; 7.0%, manufacturing, 3.9% construction; and 4.8%, other.

Of those surveyed nearly three fourths, 170 of 232, stated that the business was the owner(s) primary source of income. The sample mean for length of time the business had been in operation is 19.57 years, with a median of 13 years. The middle 50 percent of values is between 5 and 29 years.

Information on the sources used in finding employees indicates that an informal network of friends and neighbors (31.7%), walk-in applicants (17.8%), and family members of the owner or current employees (12.7%), account for 62.2 percent of new employee recruitment. State and private employment agencies (21.4%) and the other category (15.7%) accounted for the balance of recruitment.

Sample characteristics examined include the current number of full and part-time employees, the number of full and part-time employees hired in the last twelve months, the number of employees expected to be hired in the next twelve months, and the number of employees that have left the firm in the last year. A cursory examination of Table 1 reveals that the sample data are skewed to the right with mean values being significantly above medians. Therefore, the median is more useful as a measure of central tendency. The coefficient of variation for all variables in the table is greater than 100 showing a great deal of variation within the sample. However, an examination of the quartile values provides some indication of the relative magnitude of employee recruitment and retention problems. The following findings are presented for full-time employees (FTE) and part-time employees (PTE) separately. The median number of full-time employees among the firms sampled was 6 with 50 percent of the businesses having between 3 and 12 workers.

Table 1 Characteristics of Sample

Variable Sample Size Min Value Max Value Mean

Years 228 .25 108 19.57 CURR FTE 232 0 200 12.65 CURR PTE 223 0 72 3.77 HIRE FTE 229 0 200 4.72 HIRE PTE 225 0 50 3.16 EX HIR FTE 212 1 100 2.24 EX HIR PTE 216 0 100 2.08 FTE LEFT 228 0 180 3.72 PTE LEFT 223 0 50 2.17

Variable Standard 1st 2nd 3rd Deviation Quartile Quartile Quartile

Years 20.141 5 13 29 CURR FTE 21.745 3 6 12 CURR PTE 7.462 0 2 4 HIRE FTE 16.706 0 1 3 HIRE PTE 6.022 0 1 3 EX HIR FTE 8.813 0 0 1.5 EX HIR PTE 7.59 0 0 1 FTE LEFT 13.940 0 1 2 PTE LEFT 4.76 0 1 2

During the past twelve months, the median number of employees hired was one and the middle 50% was between 0 and 3. Therefore, the ratio of number of FTE hired to number of current employees is generally in the range 0/3 (O%) to 3/12 (25%) with the median being 1 of 6 (17%). The figures for PTE reveal a median of 2 employees with the first and third quartiles between 0 and 4. Since the quartile values for PTE hires are the same as for full time, the median ratio of hires in the last twelve months to number of current employees indicates that one PTE was hired on a base of 2. The third quartile shows 4 PTE with 3 hired in the last year. While this may be due to increasing use of part-time employees versus full-time or a very high PTE growth rate, it does seem to indicate that small business employee recruitment is a more important issue among firms with PTEs when compared with firms with only FTES.

Further insight into the pattern of employment growth may be gained by the expected hire categories. The median for both FTE and PTE is 0 indicating that in 50 percent of the firms hiring additional employees is not expected.

The 3rd quartile shows 1-1.5 expected hires. Therefore, new employment is not expected to show much increase.

The number of employees that left during the last year indicates a median of 1. This is one-sixth of the current FTE figure (6), but one-half of the median PTE value. This implies that retention is a more serious problem for firms with PTE when compared to those with FTE.

Reasons that employees left during the past twelve months were provided by 149 FTE and 122 PTE respondents. The full-time responses showed that finding a similar job in another company was the reason for leaving for 68 (45.6%) of the 149 FTES. Twenty-eight of the 149 FTEs (18.8%) were discharged by the employer. Firm layoffs, retirement, illness or injury, and the other categories accounted for the other 35% of full-time employee departures. The reasons for PTE employees leaving contrast with the FTE pattern. This is particularly true with respect to finding another job in a similar company. Thirty percent of FTE found similar jobs elsewhere whereas less than 15% of PTE moved to similar employment elsewhere. Interestingly, the proportion of employees that are full or part time had virtually the same percent assuming jobs in a larger company (about 15% of those who left).

Those employees who were discharged by employers were let go for the following reasons: poor job performance (40%), absenteeism (25%), dishonesty (12%), and tardiness (5%). Inability to get along with others, drug and alcohol, and other reasons comprised the balance of the responses.

Table 2 reports six hypothesis tests using the proportion for those questions which had yes or no responses. All six null hypotheses are rejected at the .01 level of significance. The conclusions supported prior expectations. Less than 40% of the small businesses studied have written job descriptions or formal performance evaluations. Less than half of all small businesses had a formal training program for employees.

Table 2 Hypothesis Tests Using the Proportion

Hypothesis Variable Sample Calculated Decision Significance Size n Z Score * = .005 ** = .001

1. Ho: pi(o)>.40 have written 231 Z = -.382 reject ** Ha: pi(o)<.40 job descriptions

2. Ho: pi(o)>.50 have formal 232 Z = -3.54 reject ** Ha: pi(o)<.50 training program

3. Ho: pi(o)>.40 have formal 230 Z = -3.78 reject ** Ha: pi(o)<.40 performance evaluation

4. Ho: pi(o)<.50 have difficulty 230 Z = 2.64 reject ** Ha: pi(o)>.50 finding quality employees

5. Ho: pi(o)<.40 have difficulty 226 Z = 3.13 reject ** Ha: pi(o)>.40 retaining quality employees

6. Ho: pi(o)<.50 use employment as 225 Z = 3.93 reject ** Ha: pi(o)>.50 stepping stone

Some key premises of this paper were that small business owners have difficulty finding and retaining quality employees, and that employees often use their small business experience as a stepping stone to employment in larger companies. The survey results supported all three of the hypotheses. More than half of the small businesses surveyed indicated that they have difficulty finding quality employees (58.7%). Just over 50% indicated difficulty in retaining quality employees, while nearly two-thirds of the respondents (63.1%) felt that employees use experience in a small business to move to a larger company. All six null hypotheses as stated in Table 2 were rejected at least at the .005 level of significance. Therefore, 99.5% confidence can be placed on these conclusions for the population of all small businesses nationally.

Information was gathered from small business owners regarding their perceptions of the greatest strengths and weaknesses of new employees. Not surprisingly, the greatest weakness in new employees was reported as lack of experience (35.7%). Lack of initiative and lack of knowledge were two other weaknesses cited by a large proportion of respondents, 23.9 and 22.6 percent, respectively. Lack of responsibility and poor attitude were other reasons mentioned.

Interestingly, the greatest strengths of new employees were a positive attitude (45.1%) and initiative (24.2%). These two responses accounted for nearly seventy percent of the total, indicating that many new employees can become valuable employees by displaying a positive attitude and showing initiative rather than being concerned about their lack of experience or knowledge of the job.

Eight X(2) tests of independence were performed to determine whether a relationship exists between the several paired variables. These results are given in Table 3. Four of the eight chi square tests reveal significant relationships between the variables, whereas four find the variables to be independent.

The first significant relationship is between type of business and source of finding employees. The calculated X(4) value is 14.018 with 8 degrees of freedom. Using a .10 level of significance one can be 90% certain that there is a relationship between the type of business and the source of finding employees. The types of business were collapsed into three categories: retail, service, and other (construction, manufacturing and all others). Five groups were used for source of finding employees. Those were: 1) friends and neighbors; 2) family members of the owner or current employees; 3) state or private employment agencies; 4) walk-in applicants; and 5) other (primarily newspaper advertising). A comparison of expected and observed frequencies reveals that retail businesses tend to rely on family members and walk-in applicants to a greater extent than other businesses. Retail businesses rely on employment agencies and newspaper advertising to a lesser degree. This rather informal approach to locating employees may be explained by the relatively low level of training generally required in retail businesses. Service businesses rely less on an informal network of friends and family and more on newspaper advertising for recruitment. Wholesale, manufacturing and construction firms use employment agencies to a greater extent and walk-in applicants to a lesser degree than do retail and service businesses.

The second and third null hypotheses could not be rejected, indicating no significant relationship between: 1) years in which the business was in operation and source of finding employees; or 2) type of business and the reason employees leave the firm.

The fourth hypothesis concerned the relationship between employment status (full or part time) and reasons for leaving.

Unfortunately, only 87 usable responses were received. The calculated X(2) statistic was 18.541 with four degrees of freedom. This is significant at a(alpha) = .001. Further analysis reveals that nearly half (49%) of the full-time employees that left did so because they found a similar job elsewhere, or in a larger company. The proportion of part-time employees leaving for these same reasons was about 38%. On the other hand, illness, layoffs or other reasons accounted for only 31% of FTE reasons for leaving versus 45% for PTE. The major reasons under the other category for PTEs was students graduating or returning to school.

The tests for independence found no relationship between type of business and the greatest strength of new employees or type of business and the greatest weakness of employees. One may assume from this data that the qualities an employer looks for in an employee are similar regardless of business type.

There were two other significant findings. The first concerns the length of time a business has been in operation and the employer's perception of the greatest strength of new employees. The chi square test of independence allows one to reject the null hypothesis of independence with an level of 10 since the calculated value of the X(2) is 14.219 with eight degrees of freedom. The raw data reveals that those businesses that have been operating for more than 15 years tend to consider experience and knowledge of the job as more important than the average for all businesses. A positive attitude appears more important for businesses that have been in existence nine years or less. This may imply that employment opportunities are better for inexperienced workers in relatively young small businesses.

Finally, the relationship between type of business and whether the employee views his/her employment as a stepping stone to employment in a larger company was tested. The chi square value was 11.402 with four degrees of freedom. Therefore, a 95% level of confidence can be placed on the statement that the type of business and whether employment in a small business is viewed as a stepping stone are related. Sample proportions reveal that construction and other, and retail firms reported 75% and 71% of their employees use small business employment as an entry to employment in large business. The proportions with this attitude are significantly less for service (56%), wholesale (44%), and manufacturing (40%).

Table 3 Chi Square Tests for Independence

Hypotheses Sample Calculated Degrees Decision Significance Size n x value of Freedom * = .10 ** = .05 *** = .01

H(1): Ho: type of busi- 225 14.018 8 reject * ness and source of finding employees are independent

H(2): Ho: years the busi- 228 12.386 16 accept ness has been in operation and source of finding employees are independent

H(3): Ho: type of business 144 9.646 12 accept and the reason em- ployees leave firms are independent

H(4): Ho: reasons em- 87 18.541 4 reject *** ployees leave and whether employeed full time are independent

H(5): Ho: type of business 206 7.549 8 accept and the employer's peception of greatest strength are indepen- dent

H(6): Ho: years the business 206 14.219 8 reject * has been in operation and the employer's per- ception of greatest strength are indepen- dent

H(7): Ho: type of business 224 9.432 6 accept and employer's per- ception of greatest weakness are indepen- dent

H(8): Ho: type of business 219 11.402 4 reject ** and employer's per- ception of whether experience is stepping stone are independent

CONCLUSIONS

The principal conclusions of this paper are as follows:

1. A ratio of the number of employees hired in the past year to number of current employees for the three quartiles ranges from 0/3 (OZ) to 3/12 (25%) for FTE, and 0/0 (0%) to 3/4 (75%) for part-time employees.

2. A ratio of number of employees that have left in the last year to number of current employees ranges from 0/3 (0%) to 2/12 (17%) for the first and third quartiles for FTEs to 0/0 (0%) to 2/4 (50%) for PTE. These first two conclusions appear to indicate that substantial proportions of small business employees are beginning and terminating their tenure with the company in any given year. A better understanding of the recruitment and retention methods and problems of small business appears desirable.

3. A prior assumption concerning small business difficulties in finding and retaining quality employees was supported. More than 50% of small businesses had difficulty finding quality employees and at least 40% were having trouble retaining them.

4. More than half of all small businesses were found to have no written job descriptions, formal training for new employees, or formal performance evaluation. While these findings are inconclusive on this issue, perhaps efforts to establish such mechanisms could help to facilitate employer-employee cooperation and improved employee

performance.

5. Employers are likely to view a new employee as an asset if they possess a positive attitude and show initiative. Lack of experience or knowledge of the job may be less important than these other characteristics, particularly in a business that has existed less than nine years.

6. Retail firms tend to rely on an informal network of friends and family for employees. This is less true of service and other types of businesses. Perhaps greater use of more formal channels for finding employees such as employment agencies or newspaper advertising would help reduce the incidence of using retail employment as a stepping stone to large business by finding employees who were really interested and qualified for the job.

7. Reasons that employees leave a business are different for full and part time. Thus, further research on the subject of small business employee retention should examine FTEs and PTEs' motivation separately.

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PSYCHOLOGICAL ANTECEDENTS OF WORK ROLE PERCEPTIONS OF BUSINESS FOUNDERS AND MANAGERS

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ABSTRACT

Perceptions of the importance of various managerial work roles are measured with a Brunswik Lens methodology. A group of CEOs who are owner-managers is contrasted with a group of nonowner-managers. The two groups differ significantly on the importance of three roles: supervision of work, technical concern with products and markets, and provision of a staff service in a non-operational area. The differences are explained in light of entrepreneurial personality traits of the owner-managers.

INTRODUCTION

One tradition of entrepreneurial research has as its focus the evaluation of factors that influence entrepreneurial careers. The factors identified can be classified into three categories:

1. Psychological factors such as need achievement (11) and control beliefs (15);

2. Personal factors such as exposure to entrepreneurial role models (3) and previous work experiences (16); and

3. Environmental factors such as capital availability (4) and skill level of the local labor market (5).

This article is intended to contribute to the literature on psychological characteristics of entrepreneurs.

Psychological Characteristics and Work Roles

The two most widely recognized psychological characteristics of entrepreneurs are need for achievement and locus of control beliefs. McClelland's early work (10, 11) established the need achievement construct as an important component of the psychological set of the entrepreneur. High achievement need is associated with a desire for personal responsibility for problem solving and the desire to reach goals through individual effort. Rotter's work (15) similarly established and stimulated research on the locus of control construct. Entrepreneurs exhibit an internal belief in the locus of control. That is, they believe they can influence the events in their lives and the rewards they obtain. The external, on the other hand, attributes much of what occurs in life to luck, fate, and other such forces outside his control.

While these are accepted components of the entrepreneur's psychological set, it is important to view them as antecedent to the entrepreneurs approach to managerial work. In this study, differences in the perceived importance of various managerial work roles between CEOs who are owner-managers and CEOs who are nonowner-managers are evaluated in light of locus of control and need achievement differences. Our objective is to determine if observed differences in work role orientation can be traced back to known psychological differences.

METHOD

Managerial Work Roles

Several categorizations of managerial work roles are available in the literature. Perhaps the best known is the partitioning of management activities presented by Mintzberg (12). However, the Mintzberg categories are not mutually exclusive, and many specific work activities can be related to more than one role. Other researchers have noted this problem in empirical settings (18).

The work roles utilized in this study were those created by Hemphill (8). He generated his set of managerial work roles by compiling a list of 575 work activities from interviewing managers and examining job description statements. This list of work activities was evaluated by 93 executives in five large manufacturing firms. Using a Likert scale, each manager rated the extent to which each statement applied to his/her job. The work roles were determined by correlating the response of pairs of the 93 subjects. Tucker's interbattery factor analysis method was applied to an off-diagonal submatrix of these intercorrelations, which generated a set of work activities that represented each work role. Reliabilities for each set of work activities ranged from .74 to .89. Low intercorrelations among the work roles indicated their relative independence. This analysis produced a set of eight work roles that would be germane to studying the position of the CEO. These roles and examples of related work activities are:

A. Providing a staff service in non-operational areas; --Selection of new employees --Assign jobs to subordinates B. Supervision of work; --Trouble shoot special operational problems as they arise --Decide the best use of available facilities C. Business control; --Review of budgets for operations --Maintenance of proper inventories D. Technical concerns with products and markets; --Assist sales people in securing important accounts --Anticipate new or changed demand for products E. Human, community, and social affairs; --Active in community affairs --Promotion of company to public F. Long-range planning; --Formulation of long-term objectives for organization --Determination of business activities to engage in G. Business reputation; --Oversees delivery schedules --Oversees the quality of company products H. Preservation of Assets --Oversees capital expenditures --Determines utilization of capital assets (8, p. xiii)

Although these work roles were formulated in 1960, they are supported by recent work on managerial behavior. In his study of managerial work behavior, Whitely (21, p. 344) notes, "Studies as widely spaced in time as Hemphill (8) and Tornow and Pinto (19) identify similar behavioral (work) dimensions."

Brunswik Lens Model

The primary thrust of this research centers on the judgment of the CEOs as to their perception of the relative importance of the managerial work roles identified with their position. One method of accomplishing this would be to simply ask each CEO to rank each work role in terms of relative importance. However, Slovic and Lichtenstein (17) established that most decision makers have poor insight when utilizing such subjective estimates of their own multiple-criteria decision process. To overcome this problem, Brunswik's Lens Model was used to study the judgment process of CEOs who are owner-managers and CEOs who are nonowner-managers.

In this model, each subject is required to make a quantitative evaluation of a large number of situations, each of which is defined by certain cue dimensions. These cue variables must be quantifiable, even if only to the extent of a 0-1 relationship. Each CEO was presented with a set of profiles ("situations"), each describing a hypothetical CEO based upon his/her ability to perform the eight work roles ("cue dimensions"). Utilizing this information the subjects rated the predicted effectiveness of each of the hypothetical CEOs. By varying two different levels of ability for each work role on each hypothetical profile, it is possible to determine the relative degree of importance that the CEO places on each work role.

This model was chosen for two reasons. First, it uses an ideographic-statistical approach to hypothesis testing, which allows for the utilization of a small sample size. Ideographic implies that each subject's behavior (judgment) must meet a statistical test of significance (6, 17). This demands that a sufficient number of situations be given to each subject to perform the appropriate statistical tests. Thus, the Lens model provides a quantified, descriptive summary of the way each CEO weighs and combines information. Second, this model, with its inferential qualities, allows the CEO to make judgments in an atmosphere that approximates his/her own decision-making environment. As Mitroff states:

The important point to appreciate about the Brunswik paradigm is that it specifically incorporates the idea of a probabilistic, uncertain decision-making environment. Unlike most psychological experiments where both the cues and the variables to be estimated are "visible," in a Brunswik experiment a subject is forced to engage in inferential decision making, i.e., to infer the value of a variable that is hidden from his "direct view." (13, p. 49) Data Collection

The research design utilized is a 4-4 split of a fixed effect 2 (8) factorial ANOVA. Each work role was described in terms of two ability levels: excellent or poor. The two levels used in this study were distributed in a 4:4 ratio. Thus, each hypothetical CEO profile has four excellent- ability work roles and four poor-ability work roles. In using such a split, the design is controlled for rater judgment bias that may occur should the profile be weighted unevenly with either more "excellent" or "poor" work role abilities.

In order to create an instrument of reasonable length, a one-half fractional replication was employed. This design produced a set of thirty-five hypothetical profiles for each subject. With instruction by the researcher, each subject made judgments as to the predicted effectiveness of each hypothetical CEO based on a scale of one to nine. For data analysis purposes, these judgments were recoded 1, 2, and 3, representing extremely ineffective, average effectiveness, and extremely effective performance.

Subjects

The subjects of this research project consisted of eight CEOs of wood furniture manufacturing firms. Four CEOs are considered owner-managers, as they started their own firms, while four CEOs were promoted to their position and are considered nonowner-managers. A single industry was selected to hold constant as many extraneous variables as possible. All firms meet the Small Business Administration's definition of "small business" in terms of dollar sales and number of employees. Each CEO was interviewed, and the data collection instrument was completed in the author's presence.

RESULTS

In Table 1, the magnitude of effect of each work role and the mean effect for each subject group are presented. These calculations are based upon the degree to which the dependent variable (i.e., "predicted effectiveness") shifted as the levels of the work role varied from poor to excellent. A positive magnitude of effect indicates the work role is important, while a negative magnitude of effect indicates the work role is unimportant. In other words, a negative magnitude of effect occurs if the predicted effectiveness variable is reduced when the level of ability goes from poor to excellent. Therefore, this index provides the "direction" and "degree" of importance of each work role.

These results indicate that three categories of work roles exist among these subjects: universally important roles, universally unimportant roles, and those roles whose importance is moderated by ownership status.

Long-range planning and preservation of assets are considered the most important roles by each group of subjects. The mean effects are statistically identical for the owners and nonowners. Neither the magnitude of importance of these roles nor the consistency across subject groups is surprising.

Table 1

Direction and Degree of Work Role Importance for Each CEO*

	Magnitude of Effect of Managerial Work Roles**							
CEO Owner-Manger	A	B	C	D	E	F	G	H
1	.188	-.058	-.062	-.076	-.326	.326	-.326	.350
2	-.188	-.247	-.188	-.012	-.198	.452	-.071	.483
3	.000	-.408	-.250	.227	-.317	.191	-.063	.666
4	-.375	-.188	-.125	.324	-.254	.381	-.127	.400
$\bar{x}$	-.094	-.225	-.156	.166	-.274	.338	-.147	.475
CEO Nonowner-Manager								
5	.125	.016	.375	-.307	-.667	-.159	-.159	.466
6	.000	-.125	-.625	-.259	-.259	.127	.127	.533
7	.357	.612	-.500	.308	-.095	-.476	-.476	.467
8	.000	-.408	-.250	-.021	-.277	.404	-.041	.485
$\bar{x}$	.125	.024	-.250	-.070	-.324	.355	-.137	.488
p value ***	.021	.005	.322	.032	.569	.873	.912	.888

* Calculation based upon the degree to which the dependent variable (predicted effectiveness) shifted as the level of the work role varied from poor to excellent. A minus (-) sign denotes a negative direction, which indicates the work role is considered unimportant.

** A: Providing a staff service in a non-operational area B: Supervision of work C: Business control D: Technical concerns with products and markets E: Human, community, and social affairs F: Long-range planning G: Business reputation H: Preservation of assets

***Scheffe's test for post hoc comparisons of each work role for each group of subjects.

Business control; human, community and social affairs; and business reputation are three managerial roles that are considered relatively unimportant by both groups of subjects. Both business control and business reputation roles involve operational activities involving inventory control, quality control, and budgetary reviews. It is likely that, even in these small firms, these activities are delegated to lower-level managers. The subjects did not perceive the work role human, community and social affairs to be important. This may be due to the geographic characteristics of the sample of firms. All of the companies were located in a rural setting that was hundreds of miles from the closest metropolitan area. Hence, there was little public and consumer visibility, and this fact may reduce the importance of this role for CEOs in this study.

Providing a staff service, supervision of work, and technical concerns with products and markets are the three roles that are perceived as significantly different in importance by the owner and nonowner groups. While clearly moderated by ownership status, our purpose here is to relate these role perceptions to the underlying psychological attributes of the owners and nonowners.

DISCUSSION

Much of the research on the psychology of entrepreneurs is directed at the identification of traits that might compel an individual to commence a business venture. The entrepreneurs in this study each formed the companies they now own and manage. Their perceptions of the importance of particular work roles differ from nonowner managers of similar firms in the same industry.

Supervision of work. Owner-managers perceive this role to be unimportant in the managerial repertoire. Indeed, except for human, community and social affairs, it was the least important of the eight roles. This result is consistent with an internal locus of control belief. Internals have been reported to be more trusting (7). Externals have been reported to favor a more directive and structured form of supervision (9, 7).

Technical concerns for products and markets. Since the owners were probably motivated to enter the furniture business due to the technical expertise or market knowledge, their continued concern for this role is not surprising. However, a high need for achievement is also consistent with this result. Direct contact with customers is likely to provide the immediate performance feedback intrinsic to the need achievement construct. Also, such behavior would assist in setting goals and supporting the sense of personal responsibility for their attainment, which is also manifest in the need achievement drive.

Providing a staff service in a non-operational area. This role is perceived as the third most important among the nonowner-managers. There is evidence that suggests managers who are promoted tend to prioritize working behaviors closely related to their former positions (1, 2, 14, 20). This may well be the best explanation for this observed difference. However, a high need for achievement among the owner-managers can also be evoked as an explanation. Staff support of a non-operational area might bear, at best, a tenuous relation to goal achievement and provide the least feedback to the owner.

In conclusion, we posit that differences in work role orientations among owners and nonowners may well be attributable to a personality set that motivates the initial entrepreneurial event. To the extent that these characteristics influence managerial work activities, they might also influence structural designs, commitments to staff development, growth strategies, and a host of other decisions subsequent to the venture formation. We view this as a logical and potentially fruitful extension of the rich history of psychological inquiry in entrepreneurial research.

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SECURITY CONSIDERATIONS IN SMALL BUSINESS COMPUTING

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ABSTRACT

Security considerations are becoming increasingly important for small businesses due to the growth in computer acquisition by small business owners as well as the increased amount of networking by these same firms. Both of these trends have created a significant increase in the potential for security problems related to the protection of proprietary information.

INTRODUCTION

The ever decreasing cost of hardware and software, an increasing quality and awareness of computer applications have generated a very high demand among small business owners for computer acquisition and implementation. Many of these computers have been or will be used in a network environment. It is estimated that over 90 percent of the mini-computers and mainframes sold or leased in the United States have communication capabilities (Shelly & Cashman, p. 82, 1980). This could be the beginning of an increase in problems related to computer security.

Computer security has become a nightmare for small business owners and managers. Protecting proprietary information, the most valuable corporate asset, is turning into a challenging and expensive task.

This is further exacerbated by computer crimes which are sensationalized and even encouraged by a happy ending on movies, television series, and fiction books. The opportunity for security problems increases due to the fact that more employees have access to computers on their job than ever with a great number of people using personal computers in their personal as well as professional lives. And more computer training is offered to small businesses, through vendors as well as educational institutions. The challenge is securing the computer system from those who want to crack the system out of curiosity as well as those who are trained criminals.

Physical security of the computer itself is not the only expense nor concern. Small business owners/managers are aware of the phenomenal price for system security devices. Computer crime has been classified as "white-collar" crime. It is a nonviolent crime in which nobody is physically hurt. In this scenario, the system intruder is trying to "beat" the system for profit and/or prestige. They often are holding a high trust position in the organization. Perhaps he/she is a disgruntled employee trying to seek revenge. Whatever the case may be, computer crime is a reality. FBI reports that the average bank robbery involves $4,200, the average bank fraud $23,500, and the average computer crime a mere half million dollars. No one knows the dollar figure of unreported computer crime, but some estimates put it as high as $3 billion a year (Capron/Williams, p. 370, 1984).

Even if a computer crime is detected, the prosecution is not assured. Several reasons would confirm this statement. First, the law enforcement officers are not fully aware of the complexities of computer related crime. Second, there are not many qualified attorneys to handle computer crime cases. Third, judges and juries are not adequately trained for the complicated computer fraud and they might not see a great value for information which has been lost and/or stolen. Finally, laws and regulations have not clearly defined the computer crime in many states.

The security issues were not of significant concern to the small business owners five years ago. The major reasons were: 1) not many small businesses owned computers; and 2) in cases having computers, they were used mostly as a stand alone system. So what does all this mean to the small business owner who is either using a computer or planning to use it in the near future? In the following pages we will discuss the major security issues related to small business computing and provide some guidelines in order to reduce the risks associated with computer utilization.

Security must be observed in the entire cycle of data processing including input part (data entry), database design, data transmission and data output.

WHY COMPUTER SECURITY IS NEEDED

Information is the most valuable asset owned by any businesses. It may range from financial data to an inventory system or even to sensitive pricing schedules. Not only is the production of timely, accurate and integrated information crucial, its maintenance is as important. This very expensive resource can be the target of unauthorized use such as divulging pricing schedules to competitors to possible destruction of data files which would be disastrous for an inventory control system. Several measures can be taken in order to secure this important asset.

As we said earlier, when a small business owner decides to acquire computer(s), there are two options available. Option one prescribes a stand alone system which is solely owned and used by a particular business. If this is the case the security issues are more controllable.

Option two is network utilization. This can be through a timeshare system, a network system within the organization, networking with other public and private databases, etc. Security difficulties are a lot more prevalent within the network environment.

TYPES OF THREATS TO SMALL BUSINESSES

There are several factors that the small business must be aware of regarding the general security issues. Some of the factors are controllable, some are partially controllable and some are totally uncontrollable. The security issues include: Fire, Natural disasters (earthquakes, flood, etc.), Theft, Software piracy, Malicious activity, Information tampering, General software security, and General hardware security.

The first step regarding security protection is to generate back-up. Each working file must be fully backed up. The back up files must be kept in a different location. The ultimate solution is diskless PC (e.g., hard disk). Even in case of hard disk, the system must be fully backed up.

Natural disasters are somewhat controllable. Building with special design for earthquake protection is now available. Potential flood damage can be controlled in most cases. Computer rooms must be separately designed. Wiring, air conditioning and fire protection should be of special concern. Different types of locks and physical protection should prevent most computer thefts. In the remaining part of this paper we will concentrate on general hardware/software security.

SECURITY MEASURES FOR SMALL BUSINESS COMPUTING

In networking environment there are two common solutions: encryption and call back modems. When encryption is used, the source data is changed to different signals (coded). At the destination point it is encoded. Call back modems, by calling the user back try to verify the validity of a particular access.

In recent years a series of biometrics have been used to protect security. These include: Fingerprint, palmprint, Hand geometry, Retinal scanning, Signature analysis, and Voice recognition.

Fingerprint is used by scanning the user's finger. Whenever a user tries to access the system his/her fingerprint will be checked against the picture stored in a file.

Palmprint: In this type the individual characteristics of the palm are used as a source of scanning for identification purposes.

Hand geometry is done by using the length of the five fingers on each hand as well as the translucence of the fingertips and the webbing.

Retinal scanning is one of the most successful methods for security protection. In this type a scanning device is contained within a binocular eye camera. Identification is verified by the stored data on the user in a computer file.

Signature analysis uses the signature of the user as well as the user's pattern, pressure deviation, acceleration and the length of the time which is needed for the user in order to sign his/her name.

Voice Recognition translates words into digital patterns for transmission to the host computer. This technique is relatively new and more research is underway.

These different techniques have been very effective. They may not be financially justified for most of the small businesses at this time. However, with rapid cost reduction and improvement in the quality, they present a viable alternative for the near future.

Token, cable shielding and room shielding are some other security measures available on the market. Token is a radio transmission device which is worn around the user's neck. The device activates the computer when the user is seated in front of the screen. After completion of the session the computer becomes inoperable. Cable shielding is accomplished by braiding layers of the conductors to form a braided shield. This scheme protects the data from any electronic leak. Room shielding is done by spraying a conductive material in the computer room.

Software security is accomplished by passwords, access codes and terminal resource security (user will be logged off after a predetermined time lapse).

Physical security is achieved by identification badges, proximity relayer door openers, corner bolts, steel encasements or electronic trackers.

There are several devices available on the market which may help to protect the security. Multisentry security devices developed by Tact Technology Corporation which are installed in front of the modem is available at a cost of $21,500 for standard 16-line version and $111,100 for the 128-line version. Security Access Multiport (SAM) is another protection device for dial- up port protection. SAM is available from LeeMAH Corporation at a cost of $450 per telephone line (Walden, 1984). Total spending on computer security devices for 1985 is estimated to be around $23 billion (Capron/Williams, P. 373, 1984).

GUIDELINES FOR INEXPENSIVE SECURITY MEASURES

Security measures can be improved with moderate expenses. To establish a comprehensive security plan inexpensively, a small business can utilize its existing resources. Following suggestions should assist the small business owner to establish some security guidelines:

1. Organize a security committee. The committee will be responsible for:

A. Setting the security policies B. Assessing the effect of system security in organization C. Distributing passwords and account numbers D. Providing security training for employees E. Establishing the necessary protection plan for the information system F. Developing a regular audit procedures for log-in and system use G. Obtaining upper-level management support for security policy enforcement H. Evaluating and revising the security policies constantly I. Labeling hardware and software with warning stickers J. Overseeing the security policy enforcement

2. Post the company's security policies on a visible place and/or in the front end of any entry port (log-in station). The signs should state the organization's policies on security.

3. Revoke terminated employee's password immediately so that a malicious employee cannot be destructive.

4. Keep sensitive data (software and printout) locked up to reduce the chance of accessing, stealing, or altering the information.

5. Exit from the program/system promptly. Log-off and turn off the machine. This would not allow an unauthorized access to the vulnerable files.

6. Limit employee access to the files in order to limit the chance for system access.

7. Limit computer access to authorized personnel only. The curious personnel will be kept away from system.

8. Alter manufacturer-installed systems access protocols to prevent any schemes directly into the operating system by past account number holders.

9. Consider unlisted telephone numbers. In some degrees, an unlisted number deters access attempts by hackers/

intruders.

10. Compare communication log against communication billing periodically. The log should contain all of the outgoing calls with the users' names and call destinations and time in and out. Also, it is recommended to keep a log of calls in and time in and out. The billing discrepancies should be investigated.

The above steps could be used as a guideline. Not every small business will need to implement every step, yet some may need to include even more steps to fit their needs.

CONCLUSION

Security protection has become a serious consideration for small business computing. The ever decreasing cost of hardware/software and improvement in networking environment has made the small business computing a more viable option. Since information is one of the most valuable commodities in any business, comprehensive and sound security measures are essential for small business computing. This paper has provided an overview of the alternative approaches to solving security problems.

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SMALL BUSINESS STRATEGY AND THE IDIOSYNCRATIC BEHAVIOR OF OWNER/MANAGERS

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ABSTRACT

The perceptions, values, beliefs and cognitive base of owner/managers have a dramatic effect on the internal behavior and strategies of small firms. Tremendous successes as well as failures have often been the result of such owner/manager idiosyncratic behaviors. This article describes how the environment, power and personality of the owner/manager combine to determine behavioral characteristics of small firms. Propositions are developed and measures to counter-balance the owner/manager's influence are suggested.

INTRODUCTION

This article suggests that in small, privately owned enterprises, the frequently idiosyncratic behavior of owner/managers greatly influences the strategic course and ultimately the success or failure of the firm.(1) The significant influence of the owner/manager on the successful or unsuccessful operation of an enterprise is a familiar topic in small business literature [4][9]. However, the affect of the peculiar behavior of owner/managers and its ultimate effect on organizational task processes, reward systems, information and decision processes, structure, goal setting, and strategy of small firms is only beginning to receive adequate discussion in the literature and recognition from business practitioners.

The definition of a small firm is subject to may interpretations. For example, number of employees, total sales, marketing territory, levels of organizational hierarchy and even amount of capitalization have all been used to distinguish a small firm. This article proposes that only one criterion indicates with fair reliability whether a business is small, fair-sized, or large. The criterion used here for determining a small firm is that the person at the top (i.e., the owner/manager) knows, without having to consult records or other associates, which persons within his organization are responsible for key results [6]. This working definition lays the groundwork for an appreciation of the significant behavioral Influence of owner/managers within small business settings.

(1) This paper recognizes that not all small entrepreneurial firms are led by "owner/managers" (Carland, et.al., 1984). The term therefore includes lead entrepreneurs of small high- growth firms, who are dominant shareholders.

FIGURE I

DETERMINING FACTORS OF BEHAVIORAL CHARACTERISTICS OF SMALL FIRMS

Nature of Environment (a) Pattern of Task Requirements (b) Technology-->Behavioral Characteristics of a Small Firm Effective Power of------------------------------------> Owner/Manager Including: organizational task processes, Personality Characteristics of----------------------->reward systems, structure, Owner/Manager goal setting, and strategy

FACTORS DETERMINING SMALL BUSINESS BEHAVIOR

The success or failure of many small businesses hinges upon the frequently idiosyncratic behavior of the owner/manager of the firm. However, few theoretical or even practical discussions of this phenomenon seem to exist. Theoretically, the organizational behavior characteristics of small firms can be seen as a combination of three sources of influence (see Figure 1). They are (a) the nature of the environment, (b) the effective power of the owner/manager, and (c) the personality characteristics of the owner/manager. These sources of influence determine the behavioral characteristics of the small firm.

Nature of the Environment

With respect to the nature of the environment, two factors that significantly affect the behavior of the small firm are patterns of task requirements and the technology employed. As small firms attempt to accomplish their selected tasks in a purposeful manner [14], each task will determine the pattern requirements of many internal behavioral responses. Depending upon the industry, product, or service the firm selects [3], the organization will discover that work patterns within the firm are a function of the type of business in which the firm engages. For instance, recurring contracts, deadlines, troubleshooting, and nonrecurrent work are examples of work pattern characteristics. Stewart [18] has identified three specific work pattern characteristics systems maintenance--characterized as recurrent, fragmented, trouble-shooting; systems administration-- characterized by recurrent time deadlines, both expected and unexpected; project-characterized as being non-recurrent, self-generating, long-term, and requiring self-attention. Mackenzie [10] has also examined the timing of internal work patterns. He suggests that work processes fall into three patterns which are: regular processes - work that continues on an ongoing basis; calendar processes - work that is only executed for specific time periods and recurs on the same time cycle (i.e., monthly, quarterly or annually) and; infrequent processes work which must be accomplished infrequently and is not on any fixed schedule. The suggestion here is that the industry, product, and/or service selected will significantly influence the dominant behavioral work patterns within the firm.

Likewise, the technology selected by the firm to achieve its tasks will also Influence its behavioral characteristics. Here the term technology is not restricted to high-tech equipment exclusively. Instead, it is recognized that the technology used to accomplish a given task can vary, for example, from manual shovels, to steam shovels, to the latest diesel-powered construction equipment. Each form of equipment simply represents technological advances in automation [16]. This notion also suggests that when the organization's selected technology changes, the behavioral requirements necessary to administer the new technology will similarly change. Therefore, it can be seen that the firm's selected industry, products and/or services determine the firm's dominant patterns of work. These work patterns will in turn influence the technologies selected to facilitate the accomplishment of the organization's work.

FIGURE 2

OWNER/MANAGER EFFECTIVE POWER IN SMALL FIRMS

Possible Power Situational Factors | | ------------------------- --------------- \|/ \|/ Decision to Use----------------->Realized Power------------------->Effective Power Possible Power

Effective Power of Owner/Manager

The effective power of the owner/manager develops as a result of his or her unique position of influence within the organization [4]. This position allows his or her opinion to carry a disproportionate amount of weight within the firm. This factor helps to explain why small firms can exhibit a large amount of idiosyncratic behavior in their organizational processes and overall strategies, reflecting the unique personality and interest biases of the owner/manager.

The idea of effective power of the owner/manager derives from earlier works of several researchers and is adapted here to the small business context [13][19]. The effective power of the owner/manager reflects his or her possible power (forces he or she can use to achieve organizational goals) and realized power (the force organizational members believe the owner/managers will use to obtain organizational goals). Thus, the owner/manager's possible power, realized power, and situational factors combine to determine effective power, the extent to which goals and objectives are actually obtained [7]. Figure 2 illustrates this relationship.

Simply stated, the primary source of the effective power of owner/managers stems from their ultimate ability to terminate the employment of organization members (threatened punishment). However, charismatic, referent, and reward power (positive reinforcement) are also frequent sources of effective power in small business settings. In other words, in small business settings, an organization member anticipates the consequences of insubordination and this anticipation acts as a constant motivation without expressive threats [16]. It is not always necessary for the owner/manager to act in order to make employees aware of expectations. Organization members will begin to anticipate the owner/manager's intentions. Based on their knowledge of the organization's culture and norms and on communication from others regarding past experiences with the owner/manager, employees will determine and adjust their own individual behaviors [7]. In summary, owner/managers typically possess considerable individual clout and the behavior of organization members is significantly shaped by the anticipated effect of their behavior on the owner/manager.

Personality Characteristics of Owner/Managers

The personality of owner/managers is important primarily because his or her perception of and responses to technology and environmentally determined work pattern requirements will significantly impact the firm's internal processes and strategy. A great deal of research has been conducted regarding the importance of individual perceptions, values and cognitive base on decision outcomes [11][15]. These selective perceptions and interpretations have a deterministic effect on strategy when top-level managers are involved [8]. The owner/ manager's perceptions, values, beliefs, competencies and incompetencies will especially effect the operations of the business. For example, he or she could incorrectly perceive required work patterns as being systems maintenance (i.e., fragmented, calling for trouble-shooting) while, it, reality, a systems administration work mode (i.e., requiring recurrent time deadlines) is the dominant work pattern the firm requires [18]. That is to say, Infrequent work processes are being utilized ineffectively when in fact calendar processes are a better "fit" with the organization's work demands [10].

Concerning technology, the owner/manager could perceive the firm's technology as being complex, when in reality relative to other organization's within the Industry, the technology is not complex. On the other hand, the owner/manager could perceive a "need" for technology that is too complex for the current problems facing the firm.(2) Such perceptual technology-reality discrepancies stem from a lack of proper training and/or experience on the part of the owner/manager and can create anxiety among an organization's members. In summary, the unique personality characteristics (i.e., perceptions, values, beliefs and cognitive base) of the owner/manager will significantly affect his or her perceptions of the firm's external and internal environments which will eventually be manifested in the firm's overall behavioral characteristics.

BEHAVIORAL CHARACTERISTICS OF THE SMALL FIRM

If the personality characteristics of the owner/manager have a disproportionate influence on selected work patterns and technology, then, the idiosyncratic preferences and behavior of the owner/ manager will also be manifested in the firm's overall behavioral characteristics and strategy. Behavioral characteristics refer to the firm's dominate organizational task processes, reward systems, information and decision processes, structure, goal setting processes and strategy.

Perceptions of the owner/manager influence organizational task processes. The decision criteria and preferences of the owner/manger limit the individual discretion of organizational employees and are reflected in the organizational task processes. For example, if the owner/manager believes that product quality or service quality is of paramount importance to the firm, then product or service quality control activities will have a dominating influence on the flow of work processes throughout the organization. Likewise, organizational reward systems will allocate greater compensation for those activities which the owner/manager believes are of greater importance. organizational decisions will be based upon what is thought to be "critical" information and data gathered during the performance of preferred activities. Stemming directly from the preferred activities, organizational structure Se also influenced by the owner/manager. If the owner/manager believes certain activities are of great importance to the firm, persons who have expertise in those "important" areas will also have greater influence within the firm. For example, if checking job related invoices and reviewing job costs are perceived as critical, then, more resources will be allocated to these activities. Eventually, this bookkeeping responsibility will evolve into a bookkeeping department, and the activities of reviewing job invoices and costs will evolve into a multifaceted accounting department. Similarly, if the activities of making calls to potential customers, advertising and sales training are perceived by the owner/manager as being "critical", then these activities would evolve into a sales or marketing department. Finally, the owner/manager's perception of "critical" will be reflected in the organization's structure as he or she personally retains control of many of these activities.

(2) For example, this frequently is manifested in an unnecessary rush to computerize current work processes as a "cure all" solution to numerous more fundamental problems.

The firm's goal setting and strategy also reflect the perceptual and cognitive biases of the owner/manager. At the inception of most small businesses, the personal goals of the owner/manager and the firm goals are typically indistinguishable. This influence of the owner/manager on the goal selection process generally continues throughout the life of the firm. The competence profile and distinctive competencies of the firm are often derived from the technical and personal competencies of the owner/manager. For instance, if the owner/manager is a product innovator, then, product innovation becomes a major goal of the firm or, the goals of the firm are stated in the context of continuing product innovation. If the owner/manager is a dynamic sales person, then, company goals will be stated in the context of increasing sales growth. Likewise, if the owner/manager is a "detail" person, a person primarily concerned with keeping tabs on accounting, this characteristic becomes a goal and distinctive competence of the firm. In essence, the goal setting processes and strategies of small firms are frequently based on the owner/manager's perception of the firm's distinctive competence, which frequently is an extension of the specific competencies (and incompetencies) of the owner/manager.

To summarize the effects of the idiosyncratic behavior of owner/managers on the behavioral characteristics of small firms, the following propositions have been developed. Hence, each individual proposition should be considered in the context of the owner/manager and the firm.

Work Pattern Requirements P1: The work pattern requirements perceived as being required by the environment will be reflected in the dominate work patterns of the firm.

Technology P2: The preferred technology will be the dominate technology of the firm.

Organizational Task Processes P3: The perceived critical processes will be the dominate work processes within the firm.

Reward Systems P4: Greater compensation will be allocated to the performance of those activities which are perceived to be of greater importance.

P5: Larger amounts of total resources will be allocated to the performance of those activities which are perceived to be of greater importance.

Information and Decision Processes P6: Larger amounts of information and data will be collected for those activities which are perceived to be of greater importance.

Structure P7: Personnel in perceptually more important areas will have greater formal authority and influence within the firm.

P8: Greater personal involvement will be exhibited in those areas which are perceived to be of greater importance.

P9: Greater personal involvement will be exhibited in those areas in which personal competence is greatest.

Goals P10: Personal goals within the firm will be indistinguishable from the firm's formally stated goals.

Strategy P11: Personal competencies (and incompetencies) will be reflected in the objectively measured distinctive competencies of the firm.

COUNTER-BALANCING THE OWNER/MANAGER

The disproportionately large amount of influence the owner/manager has on the organization's work patterns, technology, task processes, reward systems, information and decision processes, structure, goal setting and strategy can be offset and effectively counter-balanced in a number of ways. One approach is to move the small firm from an entrepreneurial process of decision- making to a more formal or professionally objective mode of decision-making. An excellent discussion of such a transition has been described by Charan, Rofer and Mahan [2].

Another approach of offsetting the effect of the idiosyncratic preferences of owner/managers is through the effective "engineering" of top management personnel and organizational staff (i.e., selection, placement, and job design requirements). For example, the managerial roles described by Mintzberg, can be generalized to small business settings [12]. The owner/manager's out-going personality characteristics may be such that he or she enjoys serving as a symbolic figurehead and liaison and is effective in doing so. This same owner/manager may be an inadequate budgeter or detail person (monitor). Or, another owner/manager may spend too much time as an idea initiator (innovator) to the detriment and neglect of other equally important organizational processes. Finally, an owner/manager's personal ineptness as a negotiator could seriously hamper the firm's profitability. The notion of organizational engineering of top management personnel and responsibilities takes into consideration the strengths and weaknesses (competencies and incompetencies) of the owner/manager as well as other management personnel.

Ideally, an objective assessment of the owner/manager's abilities along with the competencies of each member of the management team should be made within an executive group setting. Critical management task processes could then be arranged and assigned based upon the strengths and weaknesses of all of the firm's top management personnel.

The use of group settings for assessing top management personnel, arranging critical organizational activities, and assigning responsibilities for these activities focuses attention on another tool which can assist in offsetting the idiosyncratic preferences of owner/ managers. Group joint problem-solving, or other normative group problem-solving processes, can be used to offset the dominating influence of the owner/ manager's authority during regularly scheduled group problem-solving meetings. Group joint problem-solving emphasizes the continuous search for alternatives to resolve strategic issues facing the firm. The iterative search process can result in more effective overall solutions to strategic problems. Also, the process can aid in thwarting the influence of group members who might use their unique power or authority to sway solution outcomes. Thus, the group joint problem-solving procedure, or other normative problem-solving approaches, offer ways which can help to offset the overwhelming influence of the owner/manager's idiosyncratic preferences on organizational behavior and processes.

Finally, outside consultants can be of value in offsetting the unique perceptions of owner/managers. However, such outside consultants will be of greatest value if their services are requested by the owner/managers themselves.

CONCLUSION

This article, relying on Drucker's practical working definition of a small firm, outlined a framework that may help in explaining some of their behavioral characteristics. The unique characteristics that exist in many small firms call for similarly unique propositions of organizational behavior. Several such propositions have been developed here. The author agrees with Dandridge's assertion that it may be better to have two sets of organizational behavior theories. One set of theories seems appropriate for large organizations, but another set of propositions appears necessary for small organizations [5].

It is suggested that the next step would be to transform the propositions suggested here into empirically testable hypotheses. Hypotheses could then be tested in small firms of varying size, representing several industries and with varying levels of maturity or age. Such research could prove invaluable in helping to develop a greater understanding of the effect of the idiosyncratic behavior of owner/managers on small firms.

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THE STRATEGIC BUSINESS PLAN: A CONTINGENCY MODEL

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ABSTRACT

The contingency model views the evaluation of a new venture's strategy as contingent upon the nature of the key elements contained in four PERG factors (Product, Environment, Resources, and Goals) and the congruence between and among these key elements. Key elements are identified for each PERG factor. The perceived optimal generic and specific strategy is that which provides a high degree of fit among key factor elements.

INTRODUCTION

With the recognition accorded to strategic planning for its contribution to organizational effectiveness [26], it is surprising to discover the number of business plans for new ventures that lack a strategic orientation. Many plans present an unintegrated and descriptive recitation of facts, forecasts, and aspirations, leaving the task of inferring a comprehensive, coherent, and explicit strategy largely to the reader. Nor does the business plan practitioner literature, with its outline approach, stress the importance of a comprehensive strategy or, provide guidelines for the insertion of a strategic orientation [19].

Strategy is that which "links an organization to its environment in ways that lead to achievement of its goals and objectives" [28, p. 94]. It's the game plan (with attendant dollar commitments) stating how the entrepreneur intends to compete in a given business, i.e., the domain navigation strategy [5].

Figure 1 provides the PERG contingency model which can guide the preparation of a strategic business plan (SBP). The selection of a generic and specific strategy is viewed as contingent upon: 1) four PERG factors, product (P), environment (B), resources (R), goals (G); and, 2) the degree of fit between and among elements contained in each of the four PERG factors. The congruence or degree of fit among the PERG elements is represented by the double-headed arrows numbered 1 to 6. The premise of this paper is that the reader of the SBP, e.g., the venture capitalist, expects not only to find an explicit strategy, but also expects this strategy to reflect congruence across key elements surrounding each PERG factor. Congruence or 'fit' has been a key concept in the field of strategic management for over twenty years [33].

FIGURE I THE PERG CONTINGENCY MODEL

(1) PRODUCT <--------------------------------------> ENVIRONMENT /|\ /|\ /|\ /|\ (4) | | (5) | | | -- | (2)---> STRATEGY | | (6) | | \|/ \|/ \|/ \|/ RESOURCES <---------------------------------------> GOALS (3)

PRODUCT

The SBP must identify the key product (or service) elements that, along with the remaining ERG elements, will drive the strategy choice. Tyebjee and Bruno [31] report factor analysis results which indicate that venture capitalists' criteria are: product differentiation, uniqueness, profit margin/value added, patents, and competitive advantage. Porter poses the following strategic elements: 1) how will the product lower a buyer's costs or raise a buyer's performance [25, p. 53 and pp. 131-138]; 2) how will it actually be used by the buyer [25, p. 134]; 3) what characteristics of the product will determine buyer choice [24, p. 19]; 4) will the product create switching costs for the buyer [24, p. 10 and p. 21]; 5) if it is a substitute for an existing product, precisely how does it substitute and what is the relationship of the substitute's value to price as compared to the product it hopes to replace [25, pp. 273-314]. The possibility of product improvement or the development of new product features [35] and the issue of product quality [9] should be addressed. Because the time spans of product life cycles are dramatically decreasing in many industries [7], the SBP must forecast the proposed product's life cycle and the changes in PERG elements and consequent strategy that will accompany movement through the stages [30].

THE ENVIRONMENT

The proposed venture's external environment is composed of that which the firm will not be able to control directly. It presents opportunities to be exploited, threats to be neutralized, and constraints to be met. The general environmental factor (E) can be disaggregated into three levels of analysis. Key elements should be identified, in turn, for each level and the relationships between cross-level elements should be identified and analyzed. The first level is the nonproximate or macro environment [28, p. 307] presenting technological, social, cultural, political, legal, economic, demographic, and ecological conditions [10, pp. 297-306]. Tyebjee and Bruno [31] found that venture capitalists are concerned with the proposed venture's resistance to environmental threat along two macro dimensions: changing technology, and changing economic conditions which may cause cyclical sales fluctuations. Porter [25, pp. 164- 200] provides a good theoretical treatment of technological change and methods of forecasting technological evolution. Level two, the industry, is nested in level one. The use of Porter's [24, pp. 3-33] five forces model will enable the entrepreneur to discuss the inherent profitability of the industry by examining: buyer and supplier bargaining power, the threat of potential entrants, the intensity of rivalry among existing firms, and the pressure from substitute products. Use of this model will also begin to direct the choice of an optimal generic strategy to defend the new venture against the five forces. Level three, the task or proximate environment, is nested in level 2 and is composed of those forces that directly impact on the firm. Four strategic forces are considered here: the market, buyers, competitors, and suppliers. Venture capitalists focus on the elements of market need, size, growth potential, and accessibility [31]. Market/ industry segmentation is a key element including how the entrepreneur perceives the market and its segments, why a parti-

cular segment is attractive, is a new segment being created, etc. Porter [25, pp. 231-272] provides an excellent guide to segmentation. Key elements regarding the buyer are: who is the actual buyer, i.e., the specific decision maker and his/her purchasing criteria [25, pp. 140-150]; if the proposed product is a substitute or near-substitute, what is the buyer's propensity to switch, and his/her costs of switching to the proposed substitute [25, pp. 278-289]; what is the probability that customer needs or perceptions will change [25, pp. 158-160]; and, will the firm have access to intermediate buyers (distribution channels). Key environmental elements regarding competitors are: is the contemplated industry one in which no firm has a significant market share or is there a market leader [24, p. 191]; are there barriers to entry for potential competitors [31, p. 1059] [24, pp. 7-13]; if the proposed product is a substitute, how will entrenched competitors react [24, pp. 95-98; pp. 342-344]; is direct competition with larger competitors contemplated; does the targeting of multiple market segments by competitors create exploitable coordination and compromise costs for them [25, pp. 259-261]. Regarding the ease of competitor imitation of the product, MacMillan et al. [18] have developed a rationale to estimate the response time of competitors for easily imitated new products. The nature and extent of the venture's dependency upon suppliers is another important element [22], [17], [21]. Porter [24, pp. 122-125] identifies stability and competitiveness as key supplier elements.

The entrepreneur must ensure that all the relevant environmental assumptions upon which the success of the firm rest have been surfaced and tested. Stakeholder analysis [20] is an excellent technique to accomplish this task. Finally, if the forecasted environment appears uncertain, the effective SBP will include scenarios and contingency plans [25, pp. 445-481], [16].

RESOURCES

The SBP addresses three general resource elements in explicating the firm's distinctive competence: the knowledge-technique base for value creation; the capacity to acquire and generate resources; and, expertise in management along with a responsive administrative framework [15]. Major resource elements evaluated by venture capitalists are the management, marketing, financial and technical skills of the entrepreneurs and the balance of these skills [31]. Porter's five forces model can be used to surface the proposed venture's strengths and weaknesses relative to the industry [24, pp. 29-32]. Projected learning/experience curve effects [12], the possibility of future economies of scale to deter competitor entry [24, pp. 7-9] and the ability of the firm to rapidly reallocate resources in response to environmental changes [1], [11], [23] are other important resource elements.

GOALS

In addition to expecting specificity regarding the goals the entrepreneurs propose for the venture, the SBP reader(s) will attempt to discover the goals and values of the entrepreneurs and the consistency between these two goal types. Regarding the goals of the entrepreneurs, key goal elements are: does he/she wish to make money or make things [5]; is his/her primary goal to maintain control over or to grow the firm [4]; is the venture a mom and pop firm or a stable, high- payoff firm [7, p. 316]. A key goal choice for the venture is whether to maximize short-term cash flow or long-term market share [30]. Sustainable growth rate [13, pp. 97-111] and the potential influence of the entrepreneur's family objectives on the firm's objectives [27, pp. 211-217] are additional goal elements.

FACTOR CONGRUENCE

After the key elements contained in each of the four PERG factors have been identified and assigned values, they are compared across factors for degree of fit (arrows 1 to 6 in Figure 1). The optimal strategy (ex ante) is hypothesized to be that which provides the best-degree-of-fit simultaneous solution among a set of key elements. There is some empirical and theoretical support in the literature for this factor congruency hypothesis. Vesper's [34, pp. 27-55] success and failure factors for new ventures can be restated to support the congruency hypothesis. In discussing research on the success of high-technology firms, Cooper [6, p-321] notes the fit among certain R elements (multiple founders with appropriate skills, more initial capital, higher probability of the firm having a marketing function) and the product (P) and market (E) choices. Hofer [14, p. 798] hypothesizes that in the introductory stage of the product life cycle, the major determinants of business strategy are the uniqueness and quality of the product, the rate of technological change in product design, the needs of the buyer, purchase frequency, interest rates, and money supply. While the congruency of these PERG elements is not discussed by Hofer, it appears that the application of a congruency test would improve the strategy formulation process. Pitts and Snow's [23] theory can be recast in terms of the PERG contingency model: if the primary goal (G) is to build maximum market share, the entrepreneur would propose a competitive strategy based on economies of scale and experience curve effects (R), as well as market power over suppliers, customers, and competitors (E).

GENERIC AND SPECIFIC STRATEGIES

Porter [25, pp. 11-16] proposed three generic strategies: cost leadership, differentiation, and focus. Porter maintains that if the firm seeks profitability above the industry average (G), its generic strategy should be a function of the number of industry segments targeted (E) and the firm's sources of either cost advantage or differentiation. Cost advantage sources include R elements of economies of scale, proprietary technology, learning curve effects, fixed costs/capacity utilization relationships, extent of vertical integration, skill and experience of employees, etc. Among the E elements are: preferential access to raw materials, location, size of buyers served, behavior of supplier's costs, industry real growth, quality of inputs, etc. Salient P elements are product image, configuration, performance, features, ancillary services provided, etc. [25, 62-163]. Day [8, 116-118] hypothesizes that customer price sensitivity (E), customer's perceived differentiation among products on the market (E), and differences among market segments (E) significantly constrain the firm's choice of a generic strategy. Application of the PERG contingency model to the Porter and Day analyses makes explicit the need for congruence between and among PERG factor elements in generating the generic strategy.

The content of specific strategies will, of course, vary by industry and by industry segments targeted. A "real-world" example of a product-resource-environment fit was A.B. Dick's ink-jet product (P). Because the product's technological base (R) was immature, the decision was made to sell the product initially to industrial customers (E) who would tolerate reliability problems. Other markets were temporarily off limits [29]. Porter [25, pp. 150-159] discusses the translation of Stouffer's generic differentiation strategy for its frozen entree line into a specific strategy. Among the P elements mentioned were: percentage of unique dishes, attractive and consistent appearance, and brand image. Significant E elements were relationships with prime food brokers and attractive retail shelf displays. R elements discussed were: sauce technology, care in ingredient selection and preparation, and rapid restocking of shelves. This paper proposes that the process of formulating and/or evaluating Stouffer's generic or specific strategy could be improved by the addition of specific goal elements as well as by an analysis of the fit between and among key factor elements.

CONCLUSIONS

Strategy involves the dedication of resources (R) to sell a product (P) in an environment (E) in order to achieve certain goals (G). The effective business plan uses strategy as the "conceptual glue" [32] to bind together the key elements contained in the PERG factors. An optimal strategy ex ante is viewed as contingent upon key PERG elements and the extent of their fit. If, as Ansoff [2] argues, the firm's environment is becoming more turbulent and less predictable, the application of the PERG contingency model will aid in the generation of multiple preparedness strategies with flexible configurations of products (P), resources (R), and goals (G) to fit different projected environmental states (E).

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A CONTEMPORARY TOPICS COURSE IN SMALL BUSINESS

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ABSTRACT

Towards enhancing student understanding of the subject by providing practical substance for the sterile concepts of the traditional course in small business, the introduction of a companion supporting "hot issues" offering is suggested. Loosely structured, but highly responsive, it would include among its objectives: evidencing and displaying of the character of the operating environ-

ment of the field; identifying and depicting the nature of the principals to be encountered; and, clarifying and specifying the dynamics of the impinging issues.

INTRODUCTION

Curriculum relevancy was something that many students were demanding in the early 1970s. If theory could not be linked to reality, its worth was subject to question. Further, this joining, for acceptability, was something that was to be as close to instantaneous as possible --the future, especially if it was not a definitive point, was relatively unacceptable.

Initially, proposed methods for achieving juncture were more rhetorical and general than real and specific, as academics sought to cope with the emerging demands of their students for this union. Faculty curriculum committees, with full recognition of the need and having the best of intentions, had difficulty in dealing with the issue. Many feared that quick fixes, once adopted, would gain a legitimacy and permanency which could prove to be an embarrassment should relevancy subsequently be shown to be a faddish buzz-word having little or no educational significance. Others were reluctant to introduce "relevance-oriented" courses because, it was reasoned that by the time such courses were finally operationalized--academia never being noted for its speed--they could easily be obsolete.

One suggested solution, which was generally adopted and proved to be quite suitable, was the topics course technique (Haywood, 1971). It was an openly structured non-committal framework that implied neither a specific form nor a unique methodology, and offered compatibility with almost any mode of filling. An academic department, for example, could establish an all purpose course, such as "Topics in Organizational Behavior". The explicit topics would be a variable, to be selected, inserted and deleted on an ongoing contingency basis so as to best mesh with, and provide coverage of, the subject matter. A changeable descriptive modifier added to the generic course title would record and document the filling--for example, "Topics in Organizational Behavior: Leadership Styles of the Mid-1970s".

However, with the passage of time, and changes in student values, the topics course approach tended to fade from use. While still ingrained, to some extent, in the weave of the educational fabric, it is relatively no longer something that is actively sought out or readily employed. Rather, it has generally taken on the role of an expendable entity as room continues to be sought out and requisitioned for newly developing topical courses which the character of the times demand be inserted into finite curriculums.

Now relatively obscured, the topics course nevertheless continues to be a viable and supportive technique for providing substance and meaning for subjects which are treated only abstractly in principles form. Small business management, to some extent, tends to be one of these. Yet, it is an important underpinning of the private sector and something which should be fully understood and appreciated by emerging managers--be they destined to work in, or only interface with, small business.

Small business in many university communities tends to be a one-, or at best a two-, semester educational sequence--first the concepts of small business management, and second some type of supporting case work or experiential exercises. While this arrangement is certainly necessary to provide learning of the field, it may not be sufficient for a well-rounded and truly realistic appreciation of the subject--being somewhat environmentally sterile. That is to say, absent is a meaningful accompanying display of the flavor and tone of the setting in which the Principles are unfolded and the practices are played out. Comprehension of the involved technology, structure and people is important, but perhaps of equal importance is understanding within the context of the setting in which they exist.

To provide such a setting, it is suggested that consideration be given to a small business topics course. Admittedly, space would have to be found for such an offering in already crowded business programs-a cost to be paid--but the benefits to the students might well be such as to justify the expense.

Some Examples

Topics to be employed in the structuring would be selected by the instructor, based on a subjective, but informed, judgment as to those items which may well bring relevance to the conceptual material being presented in the introductory small business management course. While the availability of sufficient item would not be a problem, the small business arena being markedly more dynamic than static, culling could possibly cause some difficulty. Hence, guidelines preferably flexible and informal, would be helpful. "Relative", "Practical", and "illustrative", would be among the key words to be applied within a framework that suitably takes into account such factors as the mission of the institution, the composition of the student body, and the nature of the prevailing setting of the field.

The following four examples illustrate typical items which might well be included in such a topics course, at the time of this writing. The sampling is one of convenience and is not intended to suggest specific materials for use.

Topic A. The Unfriendly University

Small business looks upon colleges and universities as good friends--affording access to specialized equipment, providing technical assistance, and offering managerial advice. They are easy to deal with-not intimidating nor requiring a lot of time and money. Joinings are blessed by the Small Business Administration's locating, for the most part, its Small Business Development Centers and their branch offices at colleges and universities. All seems right with this coalition-- cooperation and understanding must surely abound.

Not entirely so says the National Federation of Independent Businesses, a lobbying group for about 500,000 small businesses (Jaschik, 1986). Some colleges and universities represent significant competition for small companies when they engage in the sale of goods and services not directly related to their educational mission--for example, an after-hours pizza operation run out of a dormitory kitchen, a word-processing evening training center using the school's microcomputer classroom, or a consulting service for personnel directors housed in academic department office space and using departmental clerical assistance.

It is not the increased competition that small business objects to, but rather the combination of a favorable tax position and the employment of publicly supported facilities which enables colleges and universities to price below the market rate.

Topic B. Women Entrepreneurs

In the 1970s, when women in significant numbers began to become full-time work-force members rather than home-makers, it seemed prudent to them that they take on the ways and life styles of the corporations they were entering. In particular, it appeared to be advantageous to assimilate the look and mannerisms of the executives of the executives of the firms in which they were employed, for it was with these people that they aspired to join.

However, the aspiration of some women for entry into, and advancement within, corporate life began to become somewhat jaded. For example, many women found that the probability of their reaching top level management positions in their organization was extremely small--not because they were women, but just simply that the supply of qualified people vying for the positions was so large. Too, some women became dissatisfied with the male-set operating styles of many large corporations, in that they felt that there was too much competition and not enough team play (Hencke, 1986). Efforts to change the posture, it was believed, would be long and costly-perhaps not achievable in this lifetime. Further, after discovering just what a business executive really does, and the life they lead, many women decided corporate life was not what they wanted--at least not as a setting in which to try and build a dual professional and personal life.

Many of these women, ambitious and capable, opted instead for entrepreneurship. Leaving corporations, and starting their own firms, women have established the fastest developing segment of small business. Women-owned businesses, growing about 7 percent per year--as contrasted with approximately 4 percent for men-owned companies--now total about 3 million firms (Lipper, 1986).

Topic C. Banking Plus

Commercial banks are beginning to court middle-sized companies--firms with annual sales from about $5 million to $200 million--as big company business falls off. Large organizations, for the most part, have now moved to a position of raising their money privately, using banks only for check writing and the like (Juilland, 1986).

This wooing has taken two approaches. First, banks now offer a multiplicity of low cost cash management services--such as debt defeasance, floating-rate notes, interest rate swaps, and Eurobond offerings--to attract middle-sized firms. While the costs of doing business with the mid-sized is higher than working with larger firms, mid-sized firms tend to keep more money on deposit and buy more of the item which the bank has to sell. The second strategy is to move more aggressively to become lenders to small business--hopefully generating a feeder of loyal emerging middle-sized firms. Here the effort is normally focused on pushing direct credit authority further down the organizational structure--to specialized professionals who are able to trigger the lending process (Kearns, 1986).

The desire to service the needs of small business, even if it is nothing rare or less than a marketing move to develop promising small businesses into captured middle-sized firms, provides small business with yet another avenue for funding. At the very least, it offers small firms scan opportunity to and contrast price and service offerings of the commercial banks to which they frequently turn for assistance.

Topic D. A Contemporary Assortment

(1) Parental leave legislation (S. 2278 and HR 4300, 1986) presently before the Congress, would mandate up to 18 weeks of unpaid time off , for fathers and mothers, plus job guarantees, in the case of births and adoptions. Serious child illness would extend the period to 6 months.

While firms with five or less workers would be exempt, for many small businesses this could present a serious problem. In addition to the cost of recruiting, selecting and training substitutes, there is a distinct accompanying possibility for significant losses in productivity.

(2) The Federal Office of Management and Budget, pushing for further dismantling of protective regulations and their replacement with increased measures of competition, is calling for the relaxation of the so-called "rule of two" (Competition in Contracting Act, 1984). This a formula under which the government is required to pick small-sector contractors if two or more bids have been submitted by small firms.

If promulgated, the revision could conceivably result in a number of small businesses no longer being the recipients of Federal contracts. Coupling this with a move to redefine downward the Small Business Administration's definition of a small business--500 employees-by the introduction of a new category, medium, and the potential implications of the issue heighten.

(3) In a stream of ambiguity it is generally nice to have a few stones of stability. When the Small Business Administration supports the proposition that it is nothing more than a token agency and should be eliminated, such a stand, be it justifiable or not, is perhaps more than a little distressing to scan emerging small business persons (Andrews, 1986). What they are formally seeking is certainty and consistency-not uncertainty and inconsistency. A heightened level of cognitive dissonance is perhaps one of the last things that small business folks want or need.

Government support agencies cannot be all things to all people. But, are there some things, as a minimum, that they should be? Is the longevity stance being taken by the Small Business Administration, during these deficit reduction days, reasonable and proper? And, just what is the responsibility of agencies, such as this, to the publics that they are created to serve?

Conclusions

The field of small business has become a relatively active area in the academic arena, with movement tending to be fast paced. The question of whether small business can be taught having now generally been resolved in the affirmative, consideration has advanced to the issue of how it can best be taught. Recent literature suggests such a progression and highlights the nature and tone of the delivery system discussions-Kao and Stevenson (1985) and Sexton and Bowman

(1986) for example. Surveys imply, however-Broida (1986) for instance -- that a topics course is not now among the offerings in existing programs in small business, nor apparently is it a candidate item.

While it is being proposed here that consideration should be given to a topics course -- a very specific approach-it is fully recognized that a different means with the same end would certainly be equally acceptable. Admittedly, what is fundamental is not the methodology per se but rather advancing students' abilities to think holistically-in addition to developing their skills as to how to think. The committing to memory, and the ability to recall, arrays of facts, figures and procedures is important, but only if accompanied by the aptitude to ask probing questions, reason critically, draw valid comparisons and detect reasoning fallacies. This is exactly what a good topics course does.

Logic--such as has been presented here in support of the topics ally does not convince people as to the merits of an argument. Stories or rhetoric, the art of conveying conviction without resort to logic, are normally more effective. No narratives have been presented here, however, as the intent is not a hard sell of the topics course, for there may well be techniques which are better for the intended purpose. Nevertheless, the topics course is a proven method for introducing rounding relevancy into a subject area-and it is generally ready to go.

The study of small business, while it has been on the scene for a number of years, is relatively in a basic stage of formation as a discipline. There appears to be no universally accepted model that fixes parameters, nor commonly acknowledged criteria for judging educational worth. However, a discipline has taken shape and a field has been developed. Approaches to teaching the subject, which are both effective and efficient, and are neither cast in traditional ways nor framed impractical directions, are required for achieving maturity. Bringing to pass relevance through a contemporary topics course may well be a first step.

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AN ASSESSMENT OF POTENTIAL BUSINESS INCUBATOR SERVICES: A PILOT STUDY OF EXISTING SMALL BUSINESS MANAGERS

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ABSTRACT

Small business incubators are designed to help entrepreneurs develop successful enterprises. Incubators coordinate services and financial resources and thereby reduce the start-up costs and risks which all new businesses face. Although there appears to be a growing interest in small business incubators, there is very little research among small business owners or managers regarding the services that they feel a business incubator should provide to insure that the start-up venture grows successfully into a healthy small business.

This paper is based on a pilot study of existing small business owners and managers to determine what services they feel business incubators need to provide to new businesses. Also, the study examines the assumption that different types of business (retailers, manufacturers/wholesalers and service businesses) may need different services from a business incubator.

The study was part of a joint effort by a university and community group to determine the feasibility of establishing an incubator center in a community. Small business owners/managers who had been in business four or more years in the community were interviewed by phone. Thus, the sample is based on businesses which have made it past the difficult start-up years. Their perceptions of what services a new business could use are based on their own experiences of the emerging years.

INTRODUCTION AND BACKGROUND INFORMATION

A sizeable portion of research offers evidence as to the contribution of small business to the nation's economy. For example, studies have shown that as many as two-thirds of new jobs between 1969 and 1976 in the nation's cities were created by firms with 10 or fewer employees and that 80 percent were created by businesses with fewer than 100 employees. (7) Additional studies have suggested that small firms are about twice as productive, per employee, as large organizations. (8)

Several small business studies have also indicated a high failure rate among new small businesses as well as the reasons behind these failures befalling approximately 80 percent of small businesses within their first five years. There are several reasons reported for the high failure rate among new small businesses, but the two most reported in the literature are under capitalization and poor management. (7) Local, state and federal governments as well as community organizations have tried to minimize these problems by offering financing programs. Although these resources still exist and provide some assistance to the emerging small business, another vehicle has been developed to put the new-small business in a better position to avert the traditional failure rate. This vehicle has come to be called the "small business incubator."

Proponents of the incubator concept believe such centers will lower the failure rate of new businesses by 50 percent in the first five years. (4) The Research Institute of America reports that small business incubators improve the survival odds to about 65 percent. (6)

The major purpose of the small business incubator is to nurture and develop fledgling small businesses into healthy ones. The time spent in the incubator gives entrepreneurs the time to develop the managerial skills needed to survive on their own. (2) Also, incubators can coordinate services and financial resources and thus reduce the costs and risks associated with new business enterprises for these entrepreneurs.

Although incubator centers have been around for twenty years, they have only recently begun to enjoy a surge of popularity. Of the estimated 70 small business incubators (2) in the country, close to 90 percent have come into being since 1980. (4) The structure of small business incubators can be considered quite diverse; however, some core characteristics are common to all. For example, incubators rent physical space and provide a set of logistical and management services to tenants.

Small business incubators have entry policies which are based on the objectives of the sponsoring organization which may be public, private and/or nonprofit. These entry criteria may include net jobs potential, net profit, age of the firm, space requirements, environmental considerations and economic diversification. Many incubators also have an exit policy which is usually a time limit on occupancy in the facility. This policy prevents failing or no growth companies from squandering an incubator's resources. (2)

Universities have also established small business incubators as a way to help small businesses while providing a laboratory for students in which to experience the real world of business. A major objective of university-sponsored incubators is to transfer basic research into research for new products and technologies. (7) An additional benefit which an incubator can provide universities is consulting opportunities for faculty. (3)

Services provided by the incubator to the tenant businesses may also reflect the objectives of the sponsoring organization. However, most incubators provide the following services: below market rents, on-site business assistance at low or no cost, assistance in obtaining financing, shared support services at low or no cost, flexible leases, flexible space arrangements, employee training, and clerical services. Centralized office services provided by incubators include: telephone answering, typing, copying, data processing, bookkeeping, and legal assistance. Several incubators also offer customized job training for new expanding industries through the Job Training Partnership Act. Management assistance may include assistance in developing a business plan and seminars. Financial assistance may be provided when the sponsors of the business incubator act as brokers between the new businesses and potential investors or assist in developing loan proposals. An intangible benefit is the inevitable interaction of the entrepreneur tenants. The incubator offers them opportunities to socialize, exchange ideas and experiences, and do business with each other. (5)

In a recent survey of facility managers of incubators, services provided to tenants were described by facility managers of both public and private incubators. The highest ranked services included: conference room, custodial service, photocopies, clerical services, preparation of business plans, shipping and receiving, mail service, furniture and equipment rental, government grants and loans, word processing, receptionist, lunchroom, advertising and marketing, relocation plans, research and development, and worker training. This same survey interviewed tenants regarding the services which they felt to be the most important for a firm's start-up and growth. The highest ranked services included: photocopies, conference room, receptionist, word processing, clerical, shipping and receiving, building security, accounting, preparation of business plans, equity and debt financing, government grants and loans, answering service, legal services, telephone services, telex, bookkeeping, research and development, custodial services, library, and furniture and equipment rental. (2)

In summarizing the benefits provided by an incubator to new small businesses, it is evident and logical that incubators help increase the survival rate of their tenant small businesses. Small business incubators are designed to nurture managerial skills and reduce the costs and risks for new businesses. A variety of services are offered in small business incubators, and the most common include below market rental rates, management training, and shared office space.

OBJECTIVES OF THE STUDY

The purpose of this pilot study was to determine the services that existing (four or more years) small business owner/managers feel are important for a business incubator to offer a new business tenant. In addition, perceptions of each classification of business type were compared and contrasted.

Specifically, these questions were asked: What do existing (four or more years) manufacturers/wholesalers think are the most important services that a business incubator can offer a new business tenant?

What do existing (four or more years) service businesses think are the most important services that a business incubator can offer a new business tenant?

What do existing (four or more years) retailers think are the most important services that business incubators can offer a new business tenant?

Is there a difference or similarity between the services noted by the three groups?

METHODOLOGY

A systematic random sample of 100 small business owner/managers was selected from the yellow pages of a moderately populated community in the midwest. The survey was conducted by phone over a four-week period during the summer of 1986. This was part of a joint effort by university and community organizations to determine the feasibility of establishing an incubator center in the community.

The questionnaire requested the respondents rate incubator services using a 5-point Likert scale. Respondents were asked to classify their business as retailing, manufacturing/wholesaling or specify type under the other category. In addition, questions were asked regarding the amount of time they have been in business, their number of employees, the square footage of their business, and whether they are renting or not.

RESULTS

The response rate to the telephone interviews was 39 percent. Since this was a pilot study, designed to pretest the questionnaire and determine whether or not a study on a larger scale, with a more representative sample would be appropriate, the response rate was considered acceptable. The heuristic value of the pilot study overcomes the limitations involved with a small sample size.

Table 1 shows the general characteristics of the businesses surveyed. Thirty-five percent of the businesses surveyed were retailers, 22 percent were manufacturers/wholesalers, and 43 percent were in the service industry (listed in the "other" category). Most businesses employed under ten employees and 63 percent were located in buildings under 5,000 feet.

TABLE 1

CHARACTERISTICS OF THE SAMPLE BUSINESS

Type of Business Percent

Manufacturers/Wholesales 22 Retailer 35 Other (Services) 43

Number of Employees

Under 5 39 5-10 31 11-15 10 16-20 10 21 or over 10

Approximate Square Footage

Under 5,000 63 5,000-9,999 11 10,000-14,999 9 15,000-20,000 6 Over 20,000 11

Renting

Yes 47 No 53

The aggregate of the ratings by small business managers is depicted in Table 2. The ranking of the services is based on summing the two classifications, "somewhat important" and "very important," and then arranging in numerical order from highest to lowest. As noted in the table, bookkeeping ranked highest with accounting services coming in a close second. Financial and management counseling services ranked third and fourth respectively. At the very bottom of the list were lunchrooms and on-site day care facilities.

TABLE 2

SMALL BUSINESS RATINGS OF POTENTIAL SERVICES OFFERED BY AN INCUBATOR CENTER

(1) (2) (3) (4) (5) Not Somewhat Somewhat Very Rank Service Important Unimportant Neutral Important Important

1 Bookkeeping 3% 5% 18% 31% 44% 2 Accounting Services 3 8 18 44 28 3 On-Site Financial Counseling 10 5 23 36 26 4 On-Site Management Counseling 8 13 23 36 21 5 Assistance in Finding Suitable Loans 8 10 31 21 31 6 Flexible Space Arrangements 8 18 26 36 13 7 Job Training 18 10 28 21 23 8 Flexible Leasing/ Renting Expenses 10 13 36 13 28 8 Group Health Ins. Plans 21 15 23 23 18 8 Telephone Answering 18 18 23 18 23 9 Legal Services 8 18 36 18 21 10 Word Processing 18 15 33 13 21 11 Data Processing 15 15 33 13 15 11 Typing 15 15 39 13 15 11 Office Equipment Rental 15 13 41 21 10 12 Reception Areas 21 31 21 21 8 12 Bulk Mailing Equipment 28 23 21 21 8 13 Mail Handling 23 23 26 15 13 13 WATS Lines 33 10 28 13 15 14 Office Furniture Rentals 18 18 39 18 8 15 Conference Areas 21 28 28 10 13 15 Libraries 21 36 21 15 8 16 Copying 23 15 39 10 10 17 Satellite Commun- ications 49 18 18 5 10 18 Lunchroom 55 18 21 3 3 19 On-Site Day Care Facility 56 28 14 0 3

Rank is based on rank-ordering the sum of "somewhat important" and "very important"

In determining the differences in responses by the three respondent groups (manufacturer/wholesalers, retailers, and service firms), Tables 3, 4, and 5 were created. Ratings of an incubator's potential services are presented as follows: manufacturers/wholesalers in Table 3, retailers in Table 4, and service firms in Table 5. Rankings again were based on summing the classifications of "somewhat important" and "very important" then placing in order from high to low.

TABLE 3 MANUFACTURERS/WHOLESALERS RATINGS OF POTENTIAL SERVICES (Classification of "Somewhat Important" and "Very Important" Combined)

Rank Service Percent

1 Accounting Services 16 1 Flexible Space Arrangements 16 2 On-Site Financial Counseling 15 3 On-Site Management Counseling 14 3 Job Training 14 3 Assistance in Finding Suitable Loans 14 3 Bookkeeping 14 4 Mail Handling 11 4 Copying 11 4 Data Processing 11 5 Legal Services 9 6 Group Health Insurance 8 6 Flexible Leasing 8 6 Typing 8 6 Word Processing 8 6 Office Equipment Rentals 8 6 Bulk Mailing Equipment 8 6 Conference Room 8 6 Libraries 8 7 On-Site Day Care Facilities 6 8 Telephone Answering 5 9 WATS Line 3 9 Satellite Communications 3 9 Reception Area 3

TABLE 4 RETAILERS' RATINGS OF POTENTIAL SERVICES (Classification of "Somewhat Important" and "Very Important" Combined)

Rank Service Percent

1 Bookkeeping 27 2 On-Site Financial Counseling 24 3 Accounting Services 22 4 On-Site Management Counseling 19 4 Assistance in Finding Suitable Loans 19 4 Group Health Insurance 19 5 Job Training 16 6 Flexible Leasing 14 7 Flexible Space Arrangements 11 7 Telephone Service 11 7 WATS Line 11 7 Reception Area 11 7 Office Furniture Rental 11 7 Bulk Mailing Equipment 11 8 Conference Area 8 8 Libraries 8 9 On-Site Day Care Facilities 6 10 Data Processing 5 10 Word Processing 5 10 Office Equipment Rentals 5 10 Legal Services 5 11 Lunchroom 3 11 Mail Handling 3 11 Copying 3 12 Typing 0

TABLE 5 SERVICE FIRMS' RATINGS OF POTENTIAL SERVICES (Classification of "Somewhat Important" and "Very Important" combined)

Rank Service Percent

1 Bookkeeping 35 1 Accounting Services 35 2 On-Site Management 27 2 Telephone Answering 27 3 Flexible Space Arrangements 24 3 Typing 24 3 Legal Services 24 4 On-Site Financial Counseling 22 4 Assistance in Finding Suitable Loans 22 4 Data Processing 22 4 Word Processing 22 5 Flexible Leasing 19 5 Office Equipment Rental 19 6 Job Training 16 6 Group Health Insurance Plan 16 6 Mail Handling 16 6 WATS Line 16 6 Office Furniture Rental 16 6 Reception Area 16 7 Satellite Communications 14 8 Bulk Mailing Equipment 11 9 Copying 8 9 Conference Room 8 10 On-Site Day Care Facilities 6 11 Libraries 5 12 Lunchroom 3

Bookkeeping and accounting services ranked at the top or near the top of the list among each of the three groups: manufacturing/wholesaling, service businesses and retail firms. However, manu-

facturer/wholesaler respondents ranked flexible space arrangements along with accounting services as number one. All three groups ranked on-site management counseling high on their lists.

Manufacturers/wholesalers agreed with retailers and ranked on-site financial counseling as number two. Service businesses ranked on-site financial counseling lower than the other two groups but ranked telephone answering services much higher than the others. Manufacturers/wholesalers ranked job training higher than the retailers and even higher than the service businesses. Also, finding suitable loans was ranked somewhat higher by the manufacturers/wholesalers than the other two groups. Another difference noted involved the services of mail handling and copying in which manufacturers/wholesalers ranked higher than service businesses and retailers. In fact, retailers listed these two services and typing at the bottom of their list. Retailers also listed legal services, data processing, word processing and office equipment rentals much lower than manufacturers/wholesalers and service businesses. It is interesting that typing was ranked third by service businesses, sixth by manufacturers/ wholesalers and last by retailers.

LIMITATIONS

Since the sample was drawn from the yellow pages, a problem exists with representation. Perhaps all small businesses are not listed in the yellow pages. Some may have more than one telephone. Plus there is some subjectivity involved in selecting which businesses are small.

Nonresponses were attributed to difficulties in reaching the owner/managers by phone. For many of the calls, the owner/managers were away from their office or were occupied in meetings.

Future surveys should consider this potential problem with interviewing small business owner/managers by phone. Possibly another survey technique should be implemented or one should realize that numerous call backs must occur to increase the response rate.

Of course, generalizing the results to the entire small business community is not possible. This was a pilot study based on a sample drawn from a moderately-populated, non-urban, Midwestern community.

CONCLUSIONS AND RECOMMENDATIONS

The study reaffirms that sponsors of small business incubators should be aware that tenant businesses are different in their service requirements. A thorough understanding of a particular type of business and the services they need from an incubator is essential. Perhaps an assessment of needs should be part of an incubator's entry policies. If an incubator's services do not match those needed by a potential tenant business, then the possibility for properly serving the tenant is highly questioned.

An interesting relationship can be found between this study's findings and those by King, Economus and Allen. (2) These researchers interviewed present tenants of small business incubators. Most of the services rated as important were also found to be important in this study. However, there are some differences worth noting. The top three rated services by tenant respondents were photocopies, a conference room and a receptionist. These were near the bottom of the list for this small business manager study. It seems that current business managers feel that assistance in bookkeeping, accounting, finance and management are more vital to a firm's success than the availability of photocopies, a conference room and a receptionist.

As previously stated, this study was of existing small business owner/managers who have been in business for a few years. These entrepreneurs and managers have experiences on which to base their recommendations of services which a small business incubator should offer a new business. Managers of small businesses who have made it successfully past the start-up years, are better able to base their recommendations on actual experiences versus suppositions.

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AN EMPIRICAL EXAMINATION OF RESPONSES OF SMALL BUSINESSES TO CHANGING ECONOMIC CONDITIONS: THE IMPACT ON PROFITS AND SALES

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ABSTRACT

As smaller firms are increasingly confronted by changing economic conditions, their reactions may be best to be focused on costs, prices, wages, productivity, and employment and inventory levels. Decisions about these elements are greatly enhanced for those firms which use cash plans and which supplement those plans with information gotten from consultants and trade sources.

INTRODUCTION

Over the past few years, a number of economic and government forces are being felt in the competitive environment facing the Nation's small businessman. These forces include such things as high inflation rates, high interest rates, recession and depressed markets, uncertainty of raw materials, and Government regulations and taxes. The combination of these factors can be argued to be limiting the growth of and threatening the survival of small business. As a result, many small business owners/ operators frequently blame the U.S. economy for many of their problems.

The purpose of this paper is to review the results of our study examining the relationship of the economy on small businesses and, in turn, the responses made by small firms to changes in the economy. Specifically, we examined the efforts and decisions made by smaller firms in response to "tight economic times" and the firms' efforts to control relevant variables. We also examined the reported use of cash plans and cash planning and the effect on profits and sales.

RELATED LITERATURE REVIEW

Economic Impact on Small Business

Current economic forces have a continuing impact on smaller firms of all natures, but the impact is diverse and not felt equally across types of firms. Many of these economic forces have been reported in the literature, and this information is rich in value for better understanding the impact on firms. Authors have examined and reported on the effects of such forces as inflation (16; 11); the cost and availability of capital (3); recessionary conditions and discretionary income (11); government rules, regulations, and what would seem to be increasing "intervention" in daily business activities (7; 1); respondents' ranking of problem areas and where they go to seek help and advice (14); and the effect of U.S. economic effect on the rate of business failures (6; 3); and, of course, the impact of the new tax laws on the activities of smaller firms (15). It becomes obvious that smaller firms have had to develop differing strategies for dealing with the uncertainties of these economic forces.

Strategies for Dealing with Economic Forces

Just as is the case for studies concerning the economic impact on smaller firms, there is much in the literature concerning various strategies for responding to these forces. Indeed, Chandran reminds the small business person that s/he must keep abreast of these forces in order to modify the strategic plans of the firm to meet these challenges (3, p. 34).

Not all firms can be expected to modify their plans, however; in fact, not all firms have strategic plans. Jones reported on some interesting comparisons between planning and non-planning firms (10, p. 17). Firms which plan view the firm's environment as being more restrictive yet less of a threat to the survivability of the firm. Further, firms with plans used more participation in decision making, tended to be less reactive to unanticipated changes in the environment, and apparently were more successful in their operations.

Inflation and other economic forces also force planning firms to concentrate more on cash flows and cash budgeting

(13). Yet Cooley reports that as high as 70% of the respondents in his study did not have any cash forecasts, or at best only for a short planning horizon (8, p. 4). Clute and Larson contend that this may be due to poor understanding of the procedures for and benefits of cash flow concepts, and that this--among other factors--can serve as a symptom for the prediction of business failure (6, p. 35).

Chandran reported several methods used by firms to maintain liquidity during increasing inflation. These methods included delaying loan repayments, varying credit limits, factoring, and sources of equity capital (3, p. 35). Similarly, Judd and Lee found that firms seemed to prefer a "mixed strategy" to cope with current economic conditions. This meant such strategies as reducing inventories, improving operations efficiency, personnel lay-offs, reducing prices, and reducing debt burden (11, p. 47). Vickman suggests firms should follow a four-point program including maintaining financing flexibility, using replacement cost accounting, increasing productivity of existing assets, and reviewing future growth and expansion (16, p. 6). Similarly, Omps suggests that firms should review accounting techniques to minimize taxes, review pricing policies, and implement a strong cost control program (13, p. 54).

This paper was designed to further assess the perceptions of smaller firms as to the impact of the economy on their business decisions, profits, and sales, as well as the extent of the use of cash plans/planning and cash planners on the firm's ability to respond to changing economic conditions.

METHODOLOGY

Since we wanted to examine, among other things, the effects of cash planning/planners, it was felt we needed firms large enough to possibly employ planners, yet still within the "small business" arena. Accordingly, we drew our sample from the Dunn and Bradstreet's "Million Dollar Directory" (Vol. III). This includes firms with assets between $500,000 and $999,000.

Our sample was drawn randomly, and a total of 475 questionnaires were mailed to businesses throughout the United States; 48 usable questionnaires (10.1%) were obtained. The questionnaire was administered initially to three local firms in order to establish at least primafacie evidence of adequacy.

The author-constructed questionnaire was designed to be completed without having to refer to company records. The areas examined included such things as: (1) who makes decisions involving responses to economic developments, (2) what information was most useful in making these decisions, and (3) in what areas was it felt there was much (or little) control for those decisions. Two additional areas explored were whether or not the firm had a cash plan, and where these firms obtained assistance with the problems they perceived they had with "the economy".

FINDINGS AND IMPLICATIONS

The respondents (R(s)) were first categorized by type of business activity. (See Chart 1.) It can be seen that manufacturing and retail/wholesale constituted 77% of the usable responses. Chart 2 shows the 1979-1983 sales, profits, and ranges of number of employees of the R(s). The median number of employees was 20. Most of the respondents were located in the midwest and southwest regions of the United States.

Forty-one percent of the firms surveyed had an in-house prepared cash plan. It was interesting to note that all the service firms had cash plans, whereas only 50% of the construction firms used one. The remaining 59% of those respondents did not use a cash plan, nor did 70% of all the retailers/wholesalers.

It was interesting to note that the percentage change in sales and profits from 1979-1983 did vary depending on whether or not a firm used a cash plan. For example, an average 39.4% increase in sales and a surprising 82.5% increase in profits were experienced by those firms using cash plans. On the other hand, those firms surveyed which did not use a cash plan experienced a 28% increase in sales but had a 9,7% decrease in profits during this same period!

The responding firms identified several factors that they felt impacted on their sales and the financial condition of their businesses. Recession was ranked as the major problem by 20% of the businesses. The other major problem areas, in rank order, were high interest rates, inflation, and government regulations. (See Chart 3.)

These same firms were asked to state the amount of control they had over these items. Approximately 97% of those firms citing the aforementioned factors felt that they had little or no control over them. It was interesting to note that only service and construction-type firms listed "government regulations" as having an impact on their business. Conversely, interest rates and inflation were not reported as a major concern of our service firm respondents. And whether or not a firm had a cash plan did not affect the way the firms ranked these factors.

CHART 1 COMPOSITION OF RESPONDENTS BY TYPE OF BUSINESS

Type of Firm Percentage of Responding Firms 0 10 20 30 40 50

Retail/wholesale . . . . (18) Service . . . (3) Manufacturing . . . . (19) Construction . . . . (5) Other . . . (3) n = 48

CHART 2 COMPOSITION OF RESPONDENTS BY SALES, PROFITS, EMPLOYEES (RANGES)

Years Average Type of Firm 1979 1980 1983 1979-83

Sales ($1,000) 320-253,600 100-110,000 260-120,000 272,000 Profits ($100) (800)-2,069 (5,351)-3,340 (126)-15,000 105,000 No. of Employees 2-450 3-500 4-550 mdn = 20

CHART 3 GREATEST IMPACT ITEMS BY TYPE OF BUSINESS

Factor Total Retail Service Mfg. Construction

Recession 20% 19% 33% 22% 13% High Interest Rates 16% 21% 0% 13% 20% Inflation 12% 15% 0% 9% 0% Gov't Regulations 8% 0% 22% 0% 20%

CHART 4 ITEMS OVER WHICH FIRMS FELT THEY HAD "MOST CONTROL," BY CASH PLAN/NO CASH PLAN

Factor (most control)* Cash Plan No Cash Plan

Management 18% 23% Wages 15% 7% General Productivity 0% 20%

*In descending order

The relationships between profits and the 3 most important impact factors revealed that those firms which cited inflation as having an impact on their business, profits increased 40% from 1979-1983. Those firms not citing inflation, however, had a 70% increase in profits during this same period. It may well be that firms not citing inflation were concentrating managerial efforts on elements over which they had more control, and thus, were more profitable than were those firms very concerned about inflation.

The items the respondents felt that they have the most control over were: (1) management, (2) wages, and (3) productivity. Approximately 57% of the respondents felt that they had a lot of control over these three factors. However, those firms having cash plans felt that they had more control over wages than did the non-cash plan firms. On the other hand, non-cash plan firms felt that they had more control over productivity-related factors, while firms using cash plans did not even cite this item. (See Chart 4.)

Business Strategies Practiced During Conditions of Recession/Inflation

Two questions on our survey were designed to provide insight into business strategy during a period of inflation and recession. These strategies included such options as adjusting price, costs and/or inventories. The two most common strategies reportedly used were (1) lowering cost and (2) lowering inventory. In fact, 11% of the firms citing inflation, 14% of the firms citing high interest rates, and 22% of the firms citing recession tried to reduce the effects of these economic factors by lowering costs, That is, 49% of all respondents lowered their costs in efforts to offset the impacts of inflation, rising interest rates, and recession. Another 15% of the responding firms lowered their inventory in response to adverse economic conditions.

Of those firms having cash plans, 43% lowered costs, whereas only 33% of the firms not having cash plans lowered costs, Lowering inventory was the second most popular reported strategy in non-cash plan firms. In fact, of those firms which reduced inventory, 84% of them did not follow a cash plan. Of those firms choosing to do nothing, 25% followed a cash plan, whereas 75% did not follow a cash plan. It appears that firms having and using cash plans are more reactive to a changing economy and look for ways to minimize its impact.

Comparing the three most important impact factors with the resulting business strategies, it was found that, of those firms citing inflation, over 50% of them lowered costs. In response to recession, 44% of the firms lowered costs and 22% lowered their inventory. On the other hand, those firms confronted with high interest rates either lowered costs, raised prices, or lowered inventory.

The lowering of costs was the major strategy practiced by construction firms. (See Chart 5.) The lowering of costs and "doing nothing" strategies were the major options reported by service-type businesses. Lowering inventory and raising price strategies were not practiced by service or construction firms.

Retail and manufacturing firms, on the other hand, were the only business categories that raised prices to offset economic adversities.

In conclusion, it would seem that those firms which lowered costs realized an improved profit picture more so than did those firms which lowered inventory. Specifically, from 1979-1983, those firms which lowered inventory experienced a 44% decrease in profits.

Sources of Assistance

This question addressed the issue of the "most helpful" and "least helpful" sources of assistance used by the respondents to react to changing economic conditions. Consultants and trade associations were reported as being the most helpful, while government agencies and bankers were reported as being the least helpful. (See Chart 6.)

Whether or not a firm had a cash plan did not have a significant effect on the source of assistance selected by the responding firms. That is, 44% of the firms using consultants had cash plans, whereas 64% of those firms using trade associations did not have cash plans. Surprisingly, of those firms consulting bankers, only 40% of them had cash plans. Government agencies were perceived to be the least helpful, and especially so by those firms not having cash plans. Similarly, 60% of those firms using cash plans felt that bankers were the least helpful.

The most common helpful advice given to small businesses was the lowering of costs. For example, 60% of those firms consulting a banker and 50% of those firms using trade associations felt that the advice of lowering costs was beneficial. The lowering of inventory was recommended to only 10% of the firms consulting a trade association and to only 20% of the firms which used consultants. This advice is consistent with the aforementioned finding that those firms lowering inventory experienced a 44% decrease in profits.

CHART 5 BUSINESS STRATEGY BY TYPE OF BUSINESS

Type of Strategy Business Lower Lower Costs Inventory Raise Price Do Nothing

Retail/Wholesale 41% 18% 6% 6% Service 33% 0% 0% 33% Manufacturing 50% 13% 13% 7% Construction 67% 0% 0% 0%

CHART 6 SOURCES OF HELP USED BY RESPONDENTS

Type of Trade Government Business Consultants Associations Agencies Banker

Retail 15% 7% 17% 3% Service 3% 3% 5% 0% Manufacturing 5% 15% 16% 16% Construction 0% 0% 3% 0%

Total 23% 25% 41% 19%

Conclusions

The purpose of this study was to gain insights into the perceptions held by small businesses about the impact of the economy on their businesses, as well as their felt ability to react to that impact. While our findings must be tempered by both a small sample size and a low percent of responses, some interesting findings were still noteworthy. It was found, for example, that small businesses feel that they have little or no control over the factors of recession, inflation, and high interest rates. Moreover, whether or not a firm had a cash plan did not increase the respondent's perception of control or ability to react to these factors. Cash plans did, however, have a strong positive influence on the profitability of a firm.

The small businesses surveyed felt that they had a lot of control over such factors as wages, productivity, and management. When small businesses did try to reduce the impact on their firms of the economic developments, the two most common strategies were to either lower costs or lower inventory. Firms with cash plans were more likely to lower costs or lower inventory than were firms without cash plans. Consultants and trade associations were considered to be the most helpful in assisting the small businessman. Government agencies and bankers were considered to be the least helpful, especially by firms without cash plans.

It would appear, then, that smaller firms are indeed concerned about such economic conditions as recession, inflation, and high interest rates, but they are better off focusing their decisions on costs, wages, productivity, pricing, and employment and inventory levels. To best implement those decisions, a cash plan can be considered to be a must. For assistance to react to these economic changes, the smaller firm appears to be better off calling in a consultant (or even getting information from trade associations and trade journals) rather than getting help from government agencies or, surprisingly, bankers.

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BUSINESS CONSULTING TRAMS: DOES COUNSELING THE COUNSELOR MAKE ANY DIFFERENCE?

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ABSTRACT

This paper presents the findings of a study to determine if the addition of an experienced business counselor to a student SBI project team would have a significant impact on the team's evaluation of its learning experience. The study was conducted with two sections of an SBI marketing project course. One of the sections received it's project assignment and was provided outside assistance by a SCORE counselor in addition to the SBI coordinator. The other section received guidance only from the faculty SBI coordinator. Student expectations (pretest) and reactions (posttest) were measured using a questionnaire comprised of twelve Likert-type questions. There were no significant differences between the sections. Positive student expectations regarding the SBI experience were confirmed regardless of the type and amount of support provided to them. Assistance by outside business counselors may not be warranted on the basis of improved student expectations. However, it may be justified if additional counseling support improves the quality of assistance to the business organization for which the project was conducted. Further experience with the use of outside counselors may provide insight into how the may be better used to assist project teams.

INTRODUCTION

At the present time there are over fourteen million small businesses in the U.S. Many of the innovative ideas, as well as new jobs in this country, come from small businesses. At the same time, these businesses are highly vulnerable to failure. Of those that fail, 90 percent are attributable to poor management techniques.[1]

In an attempt to provide assistance for small business firms in the United States, the Small Business Administration started the first Small Business Institute (SBI) program over 14 years ago in Lubbock, Texas. The SBI is a joint program between colleges, universities and the Small Business Administration. Through the program teams of senior and/or graduate business students provide management counseling at no cost to the client. Students typically receive academic credits for their involvement and are closely monitored by business faculty members.[2] Since the program was initiated back in 1972 SBI program have been started on over 500 university and college campuses across the United States. According to data compiled through the fall of 1983, an estimated 73,000 small enterprises had received assistance by over 220,000 students.[3] In 1984 alone over 8,600 clients were counseled by student teams from 500 colleges and universities.[4] Clients across the country are very satisfied with the student counseling effort and activity, and most effort on the part of SBI provides appears to be focused on maintaining client satisfaction.

Despite the involvement of students in the consulting process, the value of projects to the students themselves may be overlooked. For example, Lamb and Douglas have utilized the term "forgotten client" to describe students SBI program. [5] An early evaluation of the SBI program by Burr and Solomon led to the belief that the two most important SBI benefits for students are (1) the opportunity to function in a real life learning and operating environment, and (2) the opportunity to integrate theory and practice.[6] The essence of the SBI consulting experience is to establish a counseling environment which prompts the students to utilize their skills, plus seek additional sources of information. At our institution, the SBI courses are restricted to senior and graduate business majors who have had an adequate business education.

The students enroll in the SBI course with the understanding that the end result will be an oral and written report to the business client which must include practical recommendations for change. Consequently, the project helps satisfy the need and desire of students for practical "hands on experience".

In spite of the program longevity and number of clients served however, the SBI program is not without opportunities for improvement. Among the suggestions to improve SBI programs are those of Lamb and Douglas. They include a refinement of client screening procedures, a faculty monitoring profile, a stronger client awareness of their role in the consulting process, and a review of the student "free ride" tendency which occurs too often in SBI teams.[7] In addition, our experience has been that student teams need and desire additional support and counseling assistance.[8]

Firms counseled by students sometimes obtain supplemental counseling from SCORE/ACE volunteers. SCORE, the

Service Corps of Retired Executives, is a volunteer group composed of retired businessmen and women. ACE, the Active Corps of Executives is comprised of men and women actively engaged in a business career. Both groups operate under the auspices of the SBA. The philosophy of the SBA has been to endorse cooperation between SBI teams and SCORE/ACE volunteers.[9] However, little direct involvement on the part of SCORE/ACE with SBI teams seems to be the norm when one reviews management assistance options.[10] The SCORE/ACE representative, although often available, is a seldom-used source of information and assistance to SBI teams. This lack of utilization poses an interesting question, "Would student evaluations of an SBI course be significantly affected if an experienced SCORE/ACE counselor were added to the project team?" The purpose of this study was to determine if the addition of an experienced business counselor to a student project team would have a significant effect on the team's evaluation of its learning experience.

METHODOLOGY

The study was conducted with a total of 49 students enrolled in two sections of the marketing Small Business Institute course. At the beginning of the term, students were provided with preliminary information as to the nature of the course. A questionnaire was then distributed to the students to ascertain their expectations from the course. The questionnaire contained 12 statements, chosen from a larger number, which described possible expectations to be fulfilled by the course. Students were instructed to indicate the extent of their agreement with each statement by use of a six point Likert-type scale. The scale ranged from 6 (strongly agree) to 1 (strongly disagree). The instrument is shown in Exhibit 1.

Following the administration of the questionnaire, the students in each section were divided into teams of approximately four persons and assigned an SBI case. In one of the two sections, each SBI team was supplied with a SCORE counselor as an additional resource person. The counselor's experience and familiarity with the type of business organization assigned, were expected to complement student enthusiasm and abilities. The 28 students in the other section received their project assignment without provision for any outside assistance by a SCORE counselor. At the end of the term, upon completion of the project, a second questionnaire was administered to both student groups. The statements on the second instrument were essentially the same as the words on the first. The only change was to convert the statements from an expectations format to an evaluative format. The second questionnaire is shown in Exhibit 2.

ANALYSIS

Analysis of variance (ANOVA) was used for analyzing the data. The hypotheses of equal means of ratings were employed to determine if there were any significant differences between the two sections both in terms of expectations and evaluations. The results of the analysis are contained in Table 1.

A comparison of responses, as shown in Table 1, reveals no significant differences in the means of expectations between the two class sections. All of the means reflected relatively high student expectations. Similarly, there were no significant differences in the means of evaluations between the sections. Moreover, no significant differences within sections were observed between the means of expectations and those of evaluations. High student expectations were confirmed regardless of the type and amount of counselor support provided to them.

The written comments were perhaps more descriptive of the student participants feelings. They too however, were very positive with regard to both expectations and evaluations.

BEFORE

* I'm excited and slightly apprehensive going into this project, but I expect to get a lot out of it and hopefully can meet this challenge head on!

* It will be helpful to finally apply what I've learned - and to put it in a practical, day-to-day situation.

* I am hoping that this project will open my eyes to something that I've been lacking in my college education - practical experience. I'm looking forward to it.

* I'm very optimistic about this project. I think it will be a very educational experience.

* I am concerned about my abilities to solve anyone's problems - even my own. I'm hopeful this course will inspire confidence.

AFTER

* I found this class very difficult. I put in more work and effort than in any other class - however, I do feel the effort was well spent. I found the client treated us as professionals and found it to be very interesting.

* I really enjoyed the class. It was fun to apply the knowledge I've learned from my other classes.

* This project made me more aware of the real aspects involved in marketing a product and counseling a client. This was one educational experience that deemed to be very worthwhile.

* I have to admit that I wasn't very impressed with our project assignment (the project name) at first. Now, I can honestly say that I feel all the time and effort I put into this project really paid off. I also found that whatever a new product may be, the stages are usually the same.

* Possibly more guidelines at the beginning of the course would help the groups to get started faster. The first weeks of the course involve a lot of uncertainty, on where to begin or what to do.

CONCLUSION

The absence of significant differences in the study indicates that the use of SCORE counselor assistance does not noticeably affect student expectations in an SBI project. Since student expectations were high prior to the project, it would have been difficult, if not impossible, for a SCORE counselor to contribute to a positive disconfirmation of these expectations. On the other hand, the use of a SCORE counselor as a member of a student team could have created such problems as project domination by the counselor, and a "generation gap" between the counselor and team members. The absence of disconfirmation of expectations also indicates that counselor- team problems, if they existed, had no discernable negative effect on student evaluations.

From the perspective of the SBI director, the results of this study neither support nor discourage the use of experienced SCORE counselors as members of a counseling team. Student expectations represent one of a number of criteria which could be used by directors to evaluate counselor participation. Prominent among these criteria is the contribution of the SCORE counselor to the quality of assistance provided by the team to the client. This study did not evaluate this criterion. Consequently, further assessment of the use of SCORE counselors is needed to provide insight into how they may better fit into SBI counseling efforts.

EXHIBIT 1 SURVEY OF STUDENT EXPECTATIONS

Listed below are statements with which you may or may not agree. Please indicate the extent of your agreement/disagreement by checking the appropriate space to the right of each statement.

Strongly Slightly Strongly Slightly Dis- Dis- Dis- Agree Agree Agree agree agree agree 1. Project will help me to learn much about small business practices. ____ ____ ____ ____ ____ ____

2. Project will be of considerable help in learning to solve small business problems. ____ ____ ____ ____ ____ ____

3. Counseling clients will make me more aware of the variety of problems facing small business. ____ ____ ____ ____ ____ ____

4. Project will be relevant to my other classroom projects in business administration. ____ ____ ____ ____ ____ ____

5. Experience in working in a counseling group and with outside counselors will be valuable. ____ ____ ____ ____ ____ ____

6. I expect to be on the whole, very satisfied with this project. ____ ____ ____ ____ ____ ____

7. The small business manager will put into practice our group recommendations. ____ ____ ____ ____ ____ ____

8. Our recommendations will be useful to the small business(s) we counsel. ____ ____ ____ ____ ____ ____

9. I expect to receive considerable assistance from various sources of information (books, pamphlets, outside consultants, etc.) recommended by my instructor. ____ ____ ____ ____ ____ ____

10. Project will be a worthwhile addition to my college education. ____ ____ ____ ____ ____ ____

11. Project will help me put into practice what I've learned in previous courses. ____ ____ ____ ____ ____ ____

12. Project will help me learn much about counseling procedures. ____ ____ ____ ____ ____ ____

Comments:

EXHIBIT 2 SURVEY OF STUDENT REACTIONS

Listed below are statements with which you may or may not agree. Please indicate the extent of your agreement/disagreement by checking the appropriate space to the right of each statement.

Strongly Slightly Strongly Slightly Dis- Dis- Dis- Agree Agree Agree agree agree agree

1. Project helped me to learn much about small business practices. ____ ____ ____ ____ ____ ____

2. Project was of considerable help in learning to solve small business problems. ____ ____ ____ ____ ____ ____

3. Counseling clients made me more aware of the variety of problems facing small business. ____ ____ ____ ____ ____ ____

4. Project was relevant to my other classroom projects in business administration. ____ ____ ____ ____ ____ ____

5. Experience in working in a counseling group and with outside counselors was valuable. ____ ____ ____ ____ ____ ____

6. I was on the whole, very satisfied with this project. ____ ____ ____ ____ ____ ____

7. The small business manager did or will put into practice our group recommendations. ____ ____ ____ ____ ____ ____

8. Our recommendations were useful to the small business(s) we counsel. ____ ____ ____ ____ ____ ____

9. I received considerable assistance from various sources of information (books, pamphlets, outside consultants, etc.) recommended by my instructor. ____ ____ ____ ____ ____ ____

10. Project was a worthwhile addition to my college education. ____ ____ ____ ____ ____ ____

11. Project helped me put into practice what I've learned in previous courses. ____ ____ ____ ____ ____ ____

12. Project helped me learn much about counseling procedures. ____ ____ ____ ____ ____ ____

Comments:

TABLE I A COMPARISON OF GROUP MEANS OF EXPECTATIONS VS. EVALUATIONS

Section 1 Section 2 Ratio Significance Before After Before After = .05

1. Project (will help; helped) me to learn much about small business practices. 5.43 4.93 4.86 4.28 4.77 N.S.

2. Project (is; was) of considerable help in learning to solve small business problems. 5.32 4.86 4.67 4.67 2.63 N.S.

3. Counseling clients (will make; made) me more aware of the variety of problems facing small business. 5.57 5.32 5.14 4.90 3.04 N.S.

4. Project (is; was) relevant to my other classroom projects in business administration. 4.75 4.68 5.00 5.05 1.05 N.S.

5. Experience in working in a counseling group and with outside counselors (is; was) valuable. 5.71 5.50 5.43 5.38 0.33 N.S.

6. On the whole, I (expect to be; was) very satisfied with this project. 5.07 5.03 5.24 4.90 0.56 N.S.

7. The small business manager (will; did) put into practice our group recommendations. 4.41 4.52 4.76 4.57 0.73 N.S.

8. Our recommendations (will be; were) be useful to the small businesses) we counsel. 5.14 5.14 5.09 5.24 0.14 N.S.

9. I (expect to receive; received) considerable assistance from various sources of information (books, pamphlets, outside consultants, etc.) recommended by my instructor. 5.22 4.60 5.05 4.28 4.44 N.S.

10. The project (will be; was) a worthwhile addition to my college education. 5.53 5.50 5.52 5.14 2.07 N.S.

11. Project (will help; helped) me put into practice what I've learned in previous courses. 5.50 5.46 5.52 5.19 1.10 N.S.

12. Project (will help; helped) me learn much about counseling procedures. 5.11 5.17 4.95 4.71 1.60 N.S.

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BUSINESS INCUBATORS AND THE SMALL BUSINESS INSTITUTE: INTERACTIVE MODELS FOR MANAGEMENT ASSISTANCE

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ABSTRACT

Business incubator facilities are being created all across the country by both private and public sources to help start up businesses grow and survive those critical first two or three years. This paper explores the many possible relationships that can be developed between the Small Business Institute director or student teams and the incubator facility. The advantages and disadvantages of such relationships will also be analyzed.

INTRODUCTION

Both the Small Business Institutes and business incubators are involved in encouraging economic development by providing assistance to small firms that are trying to survive and grow. These organizations can provide complimentary services to such firms and avoid being placed in a competitive situation with each other. Business incubators and SBI facilities can join together to provide management assistance to new firms and work together to insure their growth and success.

INCUBATORS

Small business incubators result from an organized effort to bring together in a controlled environment new and emerging businesses by providing them with affordable and expandable space, shared office services and various forms of management assistance programs. Such facilities may be called incubators, business and technology centers, enterprise centers, or innovation centers. They may be funded either by public or private sources. They may be located in industrial sectors or on college campuses. They started springing up in the mid-to-late 1970's. There were 140 such facilities at the start of 1986 with more opening all the time. Incubator start-ups in 1986 are expected to number 100 new facilities.

Incubators provide necessary support to start up firms in four main areas. First they provide space in a multi-tenant facility. The start up firm can rent space it needs at an affordable price and at the same time have expansions options available within the same facility. This serves to keep initial overhead low and affordable. The second support comes from the existence of shared offices and services. These services range from shared specialized space such as conference rooms, cafeterias, and reception areas to shared equipment such as computers, photocopiers, word processors and audiovisual equipment to shared services such as custodial, secretarial, or professional advice. The third area of support consists of consulting services from professionals in a variety of fields such as accountants, lawyers, media specialists and financial advisors. The fourth area of support involves providing technical assistance to the start up firms often in the form of special engineering services for the development of products or manufacturing processes. An unplanned advantage of incubator facilities results from the natural interactions of the tenants. They frequently provide both technical and emotional support to each other. Many incubator facilities take on the feel of one large firm with many diverse small parts rather than many separate and distinct small units. The small start up firm can thus gain an edge by joining an incubator facility as a tenant. They can obtain the necessary space that they need in a move-in condition and receive a wide variety of support services that will encourage the growth and development of the firm and at the same time provide necessary technical, managerial and support assistance.

INTERACTIVE MODELS

There are three different models of involvement that a Small Business Institute facility can chose:

1. no direct involvement, but refer client firms to such facilities where appropriate; 2. the Small Business Institute Director is directly involved with an incubator facility as an advisor; and 3. a student team from a Small Business Institute is assigned to the incubator or to its client firms.

In the first model there is no direct relationship between the Small Business Institute and the small business incubator facility. The Director of the SBI should make all student team members aware of the existence of any local incubator facilities and the types of support services they can offer their client firms as well as the type of firms that would make a suitable tenant in such a facility. The type of tenants desired will vary from facility to facility but the information can be readily obtained from the director of the incubator facility. A start up firm may try to get started by using the home or garage of the owner and this space is often difficult to adapt for business use. A start up firm may have rented space from a commercial operation and while the space is suitable for business purposes, the firm must often rent that space in large units so the firm has high overhead when they can least afford it. A start up firm may need a variety of support services and consulting advice, but be unable to afford the cost of obtaining this help. All three are examples of the types of problems that can be solved for a start up firm by moving into an incubator facility. This can then become one of the recommendations of the team.

The second model involves the direct efforts of the Director of a Small Business Institute to serve either on the Board of Directors, the Board of Advisors or as an individual advisor to a new or existing incubator facility. Most incubator facilities have either a Board of Directors, a Board of Advisors, or both to assist in the running of the incubator facility itself as well as to help tenant firms. The SBI Director can provide the kind of expert management assistance often needed by both the incubator facility and it's tenant firms to insure their survival and growth. This affiliation can become a source of cases for the SBI and will thus lead to the development of the third model.

The third model involves the direct involvement of student teams from an SBI with either the incubator or one or more of it's tenant firms on a regular and on going basis. The incubator facility may itself be acceptable as a case for an SBI team. The incubator facility is itself a company and as such must survive and grow to continue to provide support to its tenant firms. Thus the SBI team could assist with marketing or other developmental efforts of the incubator. The SBI team could be assigned to the incubator facility to serve as an advisor or consultant to any or all tenant firms that requested such help. There may be a series of small problems that different tenant firms have, no one of which is involved enough to warrant a semester of work from a student team, but combined they offer a challenging assignment to the team.

The SBI team could be assigned to assist one firm within the incubator facility in the same manner that they could be assigned to any firm within the community that qualified for SBI help. This is the most traditional of the assistance models presented.

ANALYSIS

Why should a Small Business Institute Director be interested in exploring or adapting any of these models? Incubator facilities seem to have become in recent years the newest weapon in the arsenal of weapons used by economic development groups to spur economic growth. Studies done on existing incubator facilities seem to indicate that this sheltered environment helps firms survive long enough to develop the needed expertise to survive after they leave the incubator. Most incubator facilities have a time limit usually two or three years for a tenant firm to grow to a size where it can survive on its own. Some incubators also own industrial parks where the tenant firms can rent space after they leave the incubator facility. Thus the firm can be retained in the area and provide a source of jobs for the community. By getting involved in the incubator in one of the direct assistance models, the Small Business Institute becomes a part of the support group providing economic growth to the area. The Institute, it's director and student teams become directly involved with leaders of both the economic development and the business communities which will enhance the reputation of the Institute as a source of management assistance.

The incubator facility and it's tenant firms will provide a continuing and hopefully long term source of challenging cases for student teams to tackle. Providing assistance to start up firms is an exciting project.

Student teams can derive a real sense of satisfaction from helping a firm to start and develop. The type of business owner who chooses to locate in an incubator has already decided that they need the type of assistance such a facility provides and is thus receptive to suggestions from the student teams and is likely to put their suggestions into effect. Some incubators require that their tenants regularly participate in management assistance seminars as part of the lease arrangements. This provides easy access to all tenants for the Director and student team members. The climate generated within these incubator facilities will make the SBI team's tasks much easier. Most incubators carefully check out all prospective tenants to insure that they have the needed start up capital to last for at least a year. Some incubator facilities also provide assistance in obtaining capital funds from both public and private sources and they will also assist the firm in obtaining grant money. Thus the student team has reasonable assurance that the firm will be in existence at the end of the semester and they can thus successfully complete their case. In summary, the quality of the cases from an incubator should be high and provide a real challenge to the student teams.

CONCLUSION

Yes, Small Business Institutes should become involved with incubator facilities where they are available as this will improve the quality of cases for the students and will serve to enhance the reputation of the SBI in the local community.

ECONOMIES OF SCALE IN CREDIT UNIONS: SOME IMPLICATIONS IN AN ERA OF DEREGULATION

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ABSTRACT

This study examines economies of scale in credit unions and assesses the implication of such economies for credit union operations in a deregulated financial market environment. An application of the Benston-Bell-Murphy cost function provides evidence of the existence of economies of scale in credit unions. Deregulation has brought increased competition from other financial intermediaries and to remain viable credit unions must operate at utmost efficiency. But without significant changes in the structure of their industry, credit unions, due to their small size and localized nature, will be hard pressed to exploit such scale advantages and compete effectively.

INTRODUCTION

Credit unions are almost uniformly small financial institutions and operate in a market environment that is quite limited in scope. Unlike commercial and mutual savings banks and savings and loan associations, credit unions do not accept deposits from the general public, but only from members of the affiliated group or groups which sponsors the credit union. Members must share a common occupational, residential, or social bond.

The products or services that credit unions offer to their clients are not as extensive as the services offered by commercial banks and savings and loan associations. In the majority of cases credit unions only offer deposits and loans (12). Many credit unions are attempting to diversity their services and some now offer such attractions as share drafts, credit cards, travelers' checks, and money orders (5).

In 1985 the average credit union had 2900 members, deposits of $7 million and assets of under $8 million (13). By any measure these figures identify credit unions as being small compared to banks and S&Ls. One bank, Citibank, with assets of $176 billion has more assets than all of the credit unions in the U. S. combined (11). Given their small size the deregulation of financial institutions has important implications for credit unions. The pessimistic view is that deregulation has signaled the beginning of the end of the union industry.

Prior to deregulation credit unions were permitted to offer higher interest rates on deposits than other financial institutions and they also tended to offer loans at lower rates than the other financial institutions (9). Deregulation, of course, allows each financial institution to establish its own rates for loans and deposits. Deregulation is likely to lead to a restructuring process in which the number and size of institutions offering similar services is likely to increase. The traditional differentiated product lines offered by the various financial institutions is likely to blur. Distinct geographic market will likely become less so.

Given the small size of credit unions and the restructuring process that is likely to occur, what is the likely impact of deregulation on them? Do these developments signal the beginning of the end of credit unions or do they herald new opportunities for growth and advancement? It seems clear that if credit unions are to remain viable institutions, they must maintain an earnings stream that (1) is sufficient to pay a competitive rate of interest and (2) allows them to acquire the technical and managerial expertise that is becoming increasingly important in today's financial environment.

It is the objective of this study to analyze one aspect of credit union operations--operating costs in order to determine if cost savings due to economies of scale are possible. One popular view is that most credit unions are too small to realize any cost advantages from economies of scale. In the following section the importance of economies of scale for financial institutions is discussed. This is followed by a section describing the technique used to measure scale economies in this study. Then comes a section discussing the results derived from the model. Finally, the last section discusses some of the implications of the findings for credit unions in a deregulated financial services industry.

ECONOMIES OF SCALE IN FINANCIAL INSTITUTIONS

There have been many studies of economies of scale in commercial banks and savings and loan associations and a few studies of scale economies in credit unions. But to my knowledge, no study has attempted to assess the impact of the presence or lack thereof of economies of scale on credit union viability in an era of deregulation.

Economies of scale exist whenever a given increase in the scale of production results in a less than proportional increase in means that there are inherent cost advantages in being large. The more significant these scale economies, the greater the cost disadvantages faced by small participants in the market. In order to take advantage of economies firms must have access to a market that is large enough to permit the construction and profitable utilization of an economically-sized plant. Otherwise, it will not be possible to gain sufficient market share to realize the scale economies. This means, of course, that the presence of significant economies of scale in an industry would limit the number of firms that a given region can support.

As far as credit unions are concerned, the advent of deregulation will bring them closer toward more direct competition with other financial and intermediaries than has previously been the case. For example, during the past year credit unions have been badly battered by cut-rate car loans offered by the Big Three auto makers' financial subsidiaries. General Motors Acceptance Corporation, Ford Motor Credit Company, and Chrysler Credit Corporation have been nibbling away at the $215 billion auto loan market since they began cutting their rates back in August, 1985. From August 1985, to April, 1986, credit unions' share of the car-loan market dropped from 15.4% to 14.7% and it's still dropping (4). Auto loans have traditionally been the number one market for credit union loans.

This increase in direct competition with other financial intermediaries signals that it will be more important than ever for every credit union to operate efficiently. Such efficient operations would imply offerings interest rates on deposits that are high enough to attract and retain a suitable amount of deposits and offering loans at rates low enough to fight off any competitors who try to capture a significant share of their major loan markets. In order to achieve these twin objectives, it will be important to keep operating expenses at an absolute minimum. The presence of economies of scale would help provided that most credit unions could avail themselves of such economies.

MEASURING ECONOMIES OF SCALE

In recent literature, the Benston-Bell-Murphy cost function has emerged as an acceptable technique for analyzing costs at financial institutions 2:3. A Cobb-Douglas production function is utilized to derive the cost function in this approach. The financial institution is thus viewed as a series of physical production processes. In particular, credit unions are viewed as producing consumer loans and savings accounts.

The Benston-Bell-Murphy cost function is specified as:

C = b(o)Q^(bl)H^(b2pb3)U^(b3)

C = total operating expenses

Q = a measure of the institution's output

H = output homogeneity variables that account for the fact that Q is not a homogeneous measure.

P = miscellaneous factors such as managerial and structural differences.

U = a stochastic error term.

Note that this cost function can be written lineraly with common logarithms of variables as:

K(1) LogC = B(o) + b(1)LogQ + E i = 2

K(2) b(i)LogH(i) = E b(1)LogP(1) = u(1) i=K(1+1)

Also note that the coefficient of the output variable, b(1), is a scale parameter. If b(1) is greater than unity, there are decreasing returns to scale. If b(1) is less than unity, there are increasing returns to scale, and there are constant returns to scale if b(1) is equal to unity.

This function also assumes that output is determined exogenously and that firms minimize costs. Both of these assumptions appear to be satisfied as far as credit unions are concerned. Output is primarily a function of member demand for services and credit unions utilize a number of cost minimizing measures such as volunteer and part-time employees, payroll deductions, and subsidies from the sponsoring organization.

Implementing the Function. In this study the implementation of the Benston-Bell-Murphy equation is implemented with the following variables:

EXP + total operating expenses

NLO = number of loans outstanding

AVS = average deposit size

AVL = average size of outstanding loans

ASST = ratio of assets to members

EMPL = number of employees

VOL = number of volunteer personnel

PENR = ratio of potential members to members

PAYR = payroll deduction (yes=2, no=l)

The output of the credit union is measured by the NLO variable. Three variables are included as output homogeneity factors. These variables, AVS, AVL, and ASST, are included to compensate for size differences in the measure of output. The variables which measure managerial and structural differences are VOL, EMPL, PENR, and PAYR.

VOL is a measure of the volunteer efforts at a credit union. These unsalaried personnel should enable an institution to generate greater output at a lower cost. The PENR variable is an indicator of the tightness of the credit union's common bond. A low value for PENR indicates that an institution is successful in attracting members. PAYR is included to test whether or not there are significant administrative savings attached to a payroll deduction plan.

These variables are similar in form and type to those employed by Koot (10) and Flannery (8) in their studies of costs and economies of scale in credit unions. Operating expenses and the other operating data were collected for a random sample of credit unions in the state of Pennsylvania for 1984. Pennsylvania was chosen because its credit union industry is vibrant and well developed. It has more credit unions than any other states except California and Illinois. Over 7% of the nation's credit unions are located in Pennsylvania. By limiting the study to a small, significant, and representative portion of the national credit union population, meaningful statistical results, free of the problems of aggregation, can be obtained. Data is taken from reports supplied by Credit Union National Association.

THE ESTIMATES

Estimates of the cost function are presented in Table 1. The results show that NLO, VOL, PENR, and PAYR are significantly correlated with the credit union's operating expenses. The AVS variable is also marginally significant (at about the 60% confidence level). The results reveal that credit unions which offer a payroll deduction plan tend to have lower operating expenses. The negative sign of the penetration variable is evidence that credit unions which have achieved a high participation rate among potential members also tend to have greater operating expenses. This reflects the fact that credit unions incur expenses in selling themselves to potential members and that it costs more to maintain an institution with a high participation rate. The volunteer variable is highly significant. It measures the number of volunteer personnel who serve on the board of directors and in other staff and managerial positions.

Economies of Scale. The output variables, NLO, is highly significant. The more loans made, the greater the institution's expenses. The coefficient is also less than unity, indicating increasing returns to scale. Thus a given percentage change in output results in a less than equal percentage change in operating expenses. This is evidence that economies of scale exist with an attendant falling average cost curve over a certain range of output. The findings that economies of scale likely exist for credit unions supports the positions of Taylor (15) and Flannery (8). Taylor did not employ the Benston-Bell-Murphy function but related average total cost and average variable cost of credit unions to various output and size measures. He found that economies of scale exist.

Flannery, on the other hand, did employ the Benston-Bell-Murphy function and his empirical results did not support a case for economies of scale. However, Flannery argues that economies of scale exist but are offset by the declining degree of subsidization available to larger credit unions, and the divergence between private costs and true social costs. Koot (10) utilizing the Benston-Bell-Murphy cost function, finds strong evidence that credit unions are subject to decreasing returns to scale. However, there is some inconsistency in his results. When he uses an alternative measure of output he finds evidence of economies of scale. The results reported here use a similar output measure as Koot and find it to be compatible with increasing returns to scale.

Wolken and Navratil (16) also utilize the Benston-Bell-Murphy cost specification in a study of credit unions. They point out certain specification errors made by Flannery and Koot in their studies and that correction of these errors lead to results evidencing significant economies of scale in credit unions.

TABLE 1

REGRESSION COEFFICIENTS OF THE OPERATING EXPENSES EQUATION

Dependent Variable: Total Operating Expenses

Independent Variables Coeficients

Constant 2.1592 NLO 0.8424* R^2 = .7259 (0.1221) F-Statistic (8;64) = 21.1852

AVS 0.5040 (0.3360) Durbin-Watson Statistic = l.9792

AVL 0.0661 (0.2357)

ASST -0.1271 (0.2176)

EMPL 0.2294 (0.2156)

VOL -0.4370* (0.1844)

PENR -0.4562* (0.2025)

PAYR -0.3830* (0.0838)

Standard errors in parentheses. *Significant at the .05 level.

IMPLICATIONS UNDER DEREGULATION

The evidence from the Benston-Bell-Murphy function suggest that the per unit operating costs of credit unions decline as output increases. Hence, the potential for significant cost savings exist and such cost savings may be crucial in the credit union's fight for survival in the deregulation era. Controlling costs will enable credit unions to remain viable by making it possible for them to offer low loan rates and high savings rates.

The presence of scale economies implies that size is a desirable quantity. Therein lies the problem. In order to capitalize on the presence of such economies the majority of credit unions will have to grow and increase their market share.

Given the way the credit union industry is presently structured, this will be difficult if not impossible. Credit unions operate in a very restricted market environment. In their operations, they are restricted to accept deposits only from those persons associated with the organization which sponsors the credit union. Nation-wide credit unions are unusual and even state-wide credit unions are few in number.

Deregulation has made it possible for both bank and nonbank institutions to offer services which compete with the services offered by credit unions. In an effort to remain competitive credit unions have attempted to add an array of new services--money market accounts, savings certificates, IRA'S, credit cards, automated teller machines, mortgage loans, sharedrafts and others. All of these services have one thing in common, they add an additional cost element to the credit union. The high yield savings accounts that credit unions have added increase the cost of funds and make it necessary for credit unions to earn more and/or decrease operating expenses in order to pay such costs (16).

Changes in technology, much of it involving the application of electronics, will have tremendous significance for the financial community in the era of deregulation. The application of these new technologies to the asset exchange process has lowered the cost of collecting, storing, processing, managing, retrieving and exchanging information relating to various forms of assets and liabilities (14). Credit unions face the problem of acquiring the hardware and skilled personnel necessary for participation in this technological revolution. This will be expensive and particularly difficult for credit unions as almost all of them have only a small membership base over which to spread such expenses. Realizing the economies of scale inherent in their operations will make it possible for credit unions to acquire more of these expensive fixed assets. But ironically, the use of such technologies also tend to have economies of scale and most credit unions are too small to realize such economies individually.

The development of an electronic funds transfer system (EFTS) will also change the geographic competition of financial intermediary markets. EFTS will permit customers to deal with financial institutions over much greater geographic distances than at present (1). It will provide the opportunity for great scale economies to be realized. But credit unions with their small size and localized nature will be hard pressed to exploit such geographic and scale advantages.

The preceding analysis presents a bleak picture for credit unions. Their size and the structure of the industry will make it difficult or impossible for them to realize the economies of scale inherent in their operations and also make it difficult for them to compete effectively with other financial institutions in an era of deregulation.

If credit unions are to remain viable in the coming years, certain changes in the structure of the industry will be necessary. It seems to me that such changes would involve:

(1) An increase in the scope of the credit union market. Limiting credit union participation to the members of the sponsoring organization handicaps credit unions severely.

(2) The formation of cooperative credit union ventures is desirable. Single credit unions are hardly able to offer all of the amenities and realize the cost savings inherent in the operations of the larger financial institutions. Joint ventures among credit unions in terms of loans, purchase of capital equipment, and even the sharing of managerial personnel would allow credit unions to compete more effectively under deregulation.

(3) A continuation of the credit union's tax-exempt status is crucial. Without this advantage credit unions would conceivably have difficulty in earning enough to remain competitive.

(4) Mergers between credit unions in close proximity to one another should be permitted and actively encouraged.

(5) Allow credit unions to offer a wider range of non-depository services. These might include life insurance, brokerage services, and financial planning for non-credit union members. Such services would allow credit unions to increase their scale of operations.

Without these concessions, it is unlikely that many credit unions will be able to realize the economies of scale inherent in their structure or compete effectively once the full impact of deregulation comes to bear on the marketplace. There is a need for continued monitoring of the credit union situation and a sensitivity to their plight.

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EVALUATION OF SBDC COUNSELORS

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ABSTRACT

The Small Business Development Center program has expanded dramatically since 1976 to 355 centers located primarily at universities. Critics of this program, including the National Federation of Independent Business, have questioned the effectiveness of these programs. Their criticisms are based on low opinions of university faculty as small business counselors and dollar effectiveness of the program.

This article offers the result of surveys of Iowa SBDC clients which indicate high evaluation levels regardless of the type of counselor. It also points out that these evaluation levels increase with time spent with the client. It also points out that, despite criticisms to the contrary, SBDC clients believe that faculty counselors understand their needs. The implication for other SBDC and SBI programs is that a body of similar statistical evidence needs to be built to refute program criticism. This data would include failure rates and incremental job/sales data.

INTRODUCTION

Critics of the SBDC program were especially active in 1984 and 1985 when the future of the Small Business Administration was debated by the Reagan administration and Congress.

A strong critic of the SBDC program was the National Federation of Independent Business.

In an article appearing in the Wall Street Journal's "Small Business" section (8/5/85), Earl Hess, a spokesman for the NFIB questioned the value of the program stating that small businesses need capital, not talk. He further stated that if advice is needed, why shouldn't small business owners go to the owners of other operating businesses. The article continued with examples of SBDC cases in Georgia and Texas which indicated worthwhile assistance.

A recurring theme by NFIB speakers is that the SBDC program is not cost effective, compared to the Small Business Institute program, where student teams analyze a business and provide recommendations, or compared to the Service Corps of Retired Executives, where the advice is free and presumably more practical. These speakers do not address how these alternatives can handle the demand of 400 to 600 clients per year or whether the subjects of counseling may demand counseling specialties beyond the levels of students or a retired business person.

In the NFIB publication "Small Business Evaluates SBA", survey data of their members showed that "college/university business administration teachers" were listed as first choice for "trusted sources of management advice" by only 5% of respondents, compared to "retired business owners" (29%) and private management consultants (37%). From this they conclude that SBA management resources should be focused on private consultants and SCORE.

The first problem with this conclusion is that "business teachers" are not synonymous with SBDC counselors who are chosen from faculty and other sources for counseling abilities and background. Also, "retired business owners" are not synonymous with the membership of the SCORE organization.

As Roitman's [2] study indicates, the negative stereotypes of impractical academics persists, but the structure of questions significantly bias results. This study documented anticipated barriers between small businesses and colleges, including faculty elitism. However, 79% of these same respondents indicated a positive response to the question of whether a college could effectively provide specific managerial assistance. The second problem with the NFIB study is (their) respondent characteristics of their sample of members. Its base was heavily weighted toward larger firms (48% with gross sales over $500,000) and older firms (89% in business over 3 years). In contrast, the typical SBDC client is small (under $100,000 in sales, with under 20 employees), and new (40% - 50% are business start-ups). Therefore, surveys which purport to measure the relative effectiveness of counseling alternatives for small businesses should measure those who are most likely to need and use these services, including actual counseling clients.

Critical Issues

The critical issues appear to be:

1. Can small business owners receive practical and valuable advice from university-based programs, especially from business school faculty members?

2. Are professional consultants a significantly better source of small business counseling.

3. Are retired business owners in SCORE a significantly better source of small business counseling.

With regard to the criticism of the SBDC program as not cost effective there is a growing body of evidence [5,6,7] to the contrary.

Purpose

It is the purpose of this article to present and discuss the results of 2 surveys which attempted to measure small business owner's opinions on the effectiveness of various kinds of consultants. The analysis of these results focus on the three critical issues outlined above.

TABLE 1 1983 Survey of SBDC and Non-SBDC Clients - U.N.I.

Effectiveness Ratings of Consultants UNIVERSITY PRIVATE NON-SBDC CLIENTS SPONSORED CONSULTANT SCORE SBA

Very Effective 25.0% 30.2% 13.0% 5.6% Somewhat Effective 56.2% 53.5% 58.4% 51.9% Not Effective 18.8% 16.3% 28.3% 42.6%

RESPONSE BASE: 32 43 46 54

SBDC CLIENTS

Very Effective 25.0% 31.6% 8.0% 13.3% Somewhat Effective 70.0% 63.2% 56.0% 56.7% Not Effective 5.0% 5.3% 36.0% 30.0%

RESPONSE BASE: 20 19 25 30

TOTAL

Very Effective* 25.0% 30.6% 13.1% 8.3% Other Responses 75.0% 69.4% 86.9% 91.7%

RESPONSE BASE: 52 62 61 84

*NOTE 1: Statistically significant differences: University sponsored to SCORE, Z 1.99, interval .047, to SBA, Z 2.66, .007; Private to SCORE, Z 2.67, .0076

*NOTE 2: The response base is from respondents who used consultants in the last year. The total survey response base was composed of 88 non-SBDC clients and 52 SBDC clients with similar compositions. The overall composition was retail 32%, service 50%, and manufacturing 18%, with all groups composed primarily of firms under 30 employees (range 73%-100%) chi^2 7.558, df 4<9.49 for rejection of goodness of fit

Methodology

Two surveys were conducted. The first was conducted in 1983 by mail among 88 non-SBDC clients in Northeast Iowa and 52 clients of the University of Northern Iowa SBDC. Both samples were of familiar composition in terms of type of firm and size of firm. Both SBDC and non- SBDC firms were primarily under 30 employees (range 73% - 100%) and within one percent of each other in composition (retail, service, manufacturing). A Chi^2 goodness of fit test resulted in acceptance of the hypothesis of similar groups. Questions on the effectiveness of consultants were cross-tabbed by use of any consultant in the past year. The mail response rate was 31%.

The second mail survey was conducted in 1984 among 766 SBDC clients in 4 subcenters throughout Iowa. The response rate was 34%.

The purpose of these studies was to determine the opinion of respondents relative to the effectiveness of consultants.

Results

Table 1 shows the results of the 1983 survey for the question of effectiveness. Four types of counselors were evaluated. Although private consultants were considered "very effective" by 25% of respondents, this difference was not statistically significant with the respondent base of 52. These scores were significantly higher than the "very effective" scores of 13% for SCORE and 8% for SBA counselors. There were no significant differences between the responses of SBDC clients, although the combined "very effective and somewhat effective scores" for SBDC clients relative to university-sponsored consultants and private consultants were higher by 14% and 9% respectively.

TABLE 2

Evaluation of SBDC Assistance - 1984

By Clients - State of Iowa - 4 Centers

SOURCE OF COUNSELING

TOTAL STANDARD(1) STAFF STANDARD FACULTY STANDARD SAMPLE ERROR (%) ERROR (%) ERROR

Excellent 30.16 .0273 39.46* .0592 27.27 .0701

Very Good 30.94 .0275 29.19 .0551 31.83 .0732

Good 22.72 .0250 21.08 .0495 24.83 .0678

Fair 9.27 .0173 5.95 .0287 10.00 .0472

Poor 3.13 .0104 1.62 .0153 1.82 .0210

Very Poor 3.12 .0104 1.62 .0153 4.54 .0327

Other .65 .0048 1.08 .0125 - - ---------- ---------- ----------

TOTAL 100.00 100.00 100.00

Excellent & 61.10 .0291 68.65* .0563 59.10 .0773 Very Good

Excellent to 83.82 .0219 86.73** .0368 83.93 .0594 Good

Response 766 185 110 Base

TABLE 2 - CONTINUED

GRAD-ST. STANDARD OTHER(2) STANDARD PROFES- STANDARD (%) ERROR (outside) ERROR SIONAL (%) ERROR

Excellent 22.66 .0611 31.11 .0805 43.75 .2046

Very Good 32.03 .0680 35.56 .0833 25.00 .1786

Good 21.09 .0595 16.67 .0648 25.00 .1786

Fair 14.06 .0507 10.00 .0522 6.25 .0999

Poor 7.03 .0373 3.33 .0312 - -

Very Poor 3.13 .0254 2.22 .0256 - -

Other - - 1.11 .0182 - - ----------- ---------- ----------

TOTAL 100.00 100.00 100.00

Excellent & 54.69 .0726 66.67 .0669 68.75 .1911 Very Good

Excellent to 75.78 .0625 83.34 .0648 93.75 .0998 Good

Response 128 90 16 Base

Notes to Table

1. Standard Error at 95% confidence level, 5%, z = 1.65 * Z scores over 1.65, 5% interval for evaluation differences between consultants (Staff to Faculty & Grad. Student) 2. Includes graduated MBA's, faculty from other institutions, and University staff ** Z scores over 1.65, 5% interval for evaluation of Staff versus Grad. Students 3. Chi(2) test for excellent differences by consultant at 5% level, 4 df = 8,4 < 9,5 for acceptance of difference Chi(2) test for ex./v.g. differences by consultant at 5% level, 5 df = 2,9 < 11,1 for acceptance of difference

Table 2 shows the results of the 1984 survey on which SBDC clients were asked to rate counselors on a scale of excellent to very poor, and these responses were tabbed by type of primary counselor. The rating of excellent for the total sample was 30%, which was similar to the 25% very effective level of the 1983 survey. The only significant difference by type of consultant was the excellent score of 39.5% for staff, compared to 27.3% for faculty and 23% for grad students. The professional score of 43.7% was not significantly higher than other scores due to the low sample base of 16 who used professional consultants. Scores for excellent and very good and excellent to good showed the same differences.

The results of these surveys do not contradict the hypothesis that professional consultants are evaluated as a more effective counseling source than faculty consultants. These results simply indicate that differences in evaluation are not as wide as the NFIB study would indicate. Another study[3] by Goodwin also indicated that accountants, bankers, and attorneys were ranked higher than college professors and the SBA. But, as Hamilton[4] indicated in his criticism of the Goodwin study, "sources of information" are not the same as "sources of assistance".

It is to be expected that professional consultants would receive higher evaluations because they deal in very specific areas of their specialty, usually for very specific short-term and readily identifiable issues, such as accounting and operating problems. Faculty counselors tend to be business generalists seeking to deal in longer range, broader issues, such as management skills, organization, and planning. Professional counselors also tend to do the client's work for them on the project, compared to faculty counselors who tend to guide the client in how to do the work.

It is also to be expected that the SBDC staff consultants would receive a higher rating than faculty because they tend to act as project leaders, whose thrust is total project completion, as opposed to subsections of the project. The staff is also more likely to have operating knowledge of specific businesses, due to their business backgrounds. As further evidence of the importance of contact with consulting sources to provide a realistic evaluation, Table 3 indicates that evaluation scores of excellent (40%) and excellent to good (89%) were significantly higher among clients who spent over 12 hours with that counselor. It is also an indication that the productive benefits of SBDC or any other kind of consulting are far greater on a long term basis.

TABLE 3 1984 SBDC Survey - Iowa

Evaluation of Hours of Counseling Z Score Assistance Under 12 Hours Over 12 Hours Interval % Stand. Error* % Stand. Error*

Excellent 28% .0300 40% .0647 2.92 (.0035) Very Good 32% .0312 27% .0586 1.22 (.2225) Good 23% .0281 22% .0547 .31 (.7566) Fair 10% .0200 6% .0314 1.69 (.0910) Poor 3% .0114 3% .0225 - - Very Poor 3% .0114 3% .0225 - - Other .8% .0060 Excellent/ 60% .0327 67% .0621 1.60 (.1096) Very Good Excellent to 83% .0251 89% .0413 1.77 (.0767) Good

BASE 610 156

* at Z=1.65, 95%, 5% range

Chi(2) Test: null hypothesis of no difference, df 1, Chi(2) 3.84 Excellent, Chi(2) = 6.0 not accepted Excellent/Very Good responses, Chi(2) = 1.02, accepted

TABLE 4 EVALUATION OF SBDC ASSISTANCE (1984) By Clients - University of Northern Iowa Compared to Other Iowa University Centers

OTHER EXCEL- STAN- EXCELLENT/ STAN- IOWA % LENT DARD VERY GOOD DARD SBDC'S CLIENTS RATING ERROR RATING ERROR BASE

TOTAL 100% 29% .0364 61% .0392 422

Staff 33% 39%* .0668 67%* .0663 137 Faculty 19% 22% .0759 52% .0908 81 Graduate Student 27% 21% .0624 54% .0764 116 Other 20% 31% .0828 66% .0848 85 Professional 1% 0% 50% .5834 2

U. N. I.

TOTAL 100% 42% .0784 70% .0728 108

Staff 44% 40% .1167 73% .1057 48 Faculty 27% 41% .1507 65% .1461 29 Graduate Student 11% 42% .2351 75% .2063 12 Other 5% 40% .3615 80% .2952 5 Professional 13% 50% .2651 71% .2001 14

* Z scores over 1.65, 5% interval for evaluation differences between consultants; Excellent: Staff to Faculty 2.61, .009; Staff to Grad. Student 3.05, .003 Excellent/Very Good: Staff to Grad Student 2.09

Excellent: Total U.N.I. to other Z 2.55, .009; Faculty Z 1.99, .05

Excellent/Very Good: Total U.N.I. to other Z 1.82, .07

CHI(2)tests for differences among consultants at 5% level for acceptance of hypothesis of differences Other Iowa SBDC'S: 11.75 >5.99 for acceptance; df 2 U.N.1 SBDC: .05< 7.81 for acceptance; df 3 Other SBDC's to U.N.I.: 4.32> 3.84 for acceptance; df 1

Outside professionals are drawn in for technical and manufacturing issues and specific assistance related to the preparation of advertising/sales brochures. It is our supposition that, by removing the unfair expectation that a faculty or graduate student consultant should be able to discuss in detail all aspects of the client's operation and quickly provide detailed recommendations on those aspects, the evaluation of those consultants will be higher and more fairly represent their abilities.

It is also important to note that evaluation "scores" of SBDC centers will vary, but that it would be expected that on the whole the excellent/very good scores would exceed minimum levels of 50%. For instance Table 4 shows the difference in scores" by type of counselor between our university's SBDC center and 3 other Iowa centers. There was a significant difference in the excellent and excellent/very good scores between our center and other centers, but this difference was not primarily due to the different mix in type of consultants (more professional and staff than faculty/grad students) but due to higher evaluation scores for faculty and graduate students. It is our supposition that these "score" differences are due to differences in the scope of consulting and not due to "quality" differences. For example, graduate student counseling at our center is primarily centered upon computer pro-forma generation, research assistance, and recordkeeping assistance. Faculty counseling is primarily centered on accounting problems, specific managerial performance areas (supervisory improvement, feasibility/strategic planning M.B.O.'s, job definitions), and other specific portions of the total project. Staff counseling is centered upon total project completion/ coordination, marketing/advertising issues, and business plan preparation.

TABLE 5

1984 SBDC Survey-Iowa

Counselor Understanding of Client Needs

GRAD FAC- STUD- PROFES- STAFF S.E. ULTY S.E. DENT S.E. OTHER S.E. SIONAL S.E. TOTAL

Yes 86.5% (.041) 80.7% (.062) 72.3% (.065) 81.5% (.067) 93.7% (.100) 81.2% No/Not Sure 13.5% 19.3% 27.7% 18.5% 6.3% 18.8% --------- ----------- ------------ ----------- ----------- ----------- Total 100.0% 100.0% 100.0% 100.0% 100.0% 100.0%

Base 185 109 130 92 16 33

Significant Z scores: Staff to Grad. Student: Z = 3.13, .0019 Grad. Student to Professional Z = 1.86, .0629 All other Z scores under 1.65

CHI(2) test for differences in understanding by consultants at 5% level, 5 df - 2.4 < 12.6 for acceptance of difference

The 1984 survey also tends to refute the criticism that faculty consultants don't have the appropriate backgrounds to truly understand small business owner needs. Table 5 indicates that 81% of respondents who used primarily faculty counselors answered yes to the question on understanding of client needs, which was equal to the overall sample of 81%. The only significant differences in response were between staff counselors (86%), graduate students (72%), and professional consultants (94%).

Other Measures of Effectiveness

Statistics have been provided from articles by Robinson [5,6] on the basis of surveys of Georgia SBDC clients showing higher increases in profitability and sales among SBDC firms versus non- firms and incremental tax revenue from SBDC clients, which indicate high multiples of program payback. Our own study [7] using different methodology, a larger sample base, and different projection methods, confirms the basic premises of the Robinson studies. The NFIB dismisses these studies as "a lot of fancy bean counting" but have yet to meaningfully elaborate on the faults of the studies, submit statistics which refute the studies, or offer studies to indicate more cost effective and realistic alternatives. Their contentions that the SBI (Small Business Institute) and SCORE programs are more efficient begs the articles by Robinson on the basis of question, since free counseling will always be cheaper than paid counseling. Even if all management assistance programs were equal in quality and all programs were appropriate for any client need, regardless of sophistication and complexity, the question of handling capability remains. SBI and SCORE programs cannot handle 400 to 600 clients per location per year. Suggestion by NFIB spokesmen that these prebusinesses or existing businesses should find and consult with owners of operating businesses are not realistic. Even if the appropriate operating owners can be found who would have the specific business management knowledge, how many would be willing to spend five to twenty-five hours working with another small business owner, for little or no compensation, in light of time pressures? The NFIB spokespeople tend to confuse "problems" with management knowledge and decision making, as if psychological support from peers is the function of counseling.

Summary and Conclusion

From the findings of these surveys, it can be concluded that university-based counseling is a viable source of management assistance that meets with client approval. The opinions about faculty counselors among those with no contact with those counselors can vary widely depending on question bias. Among those small business owners who do have contact with faculty and other types of SBDC counselors, there are relatively small differences in approval ratings. We believe, but have no statistical evidence, that these approval "scores" can be influenced by how these faculty counselors are used in terms of scope of consulting and project completion responsibilities. Further evaluations of this type, using job generation/sales increase/failure reduction measures, are needed not only to silence critics, but to improve and monitor management assistance program performance.

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EFFECTIVE WAYS TO DEVELOP SMALL BUSINESS EXPORTS: THE VIEWS OF SMALL MISSOURI FIRMS INVOLVED IN FOREIGN TRADE

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ABSTRACT

Passage of the Export Trading Company Act of 1982, small business set-asides at the Export- Import Bank, and Small Business Administration awards to successful small business exporters illustrate federal interest in foreign trade for small business. States have sought to complement the federal effort. Forty states, for example, spent an estimated $25 million in 1985 promoting exports (11). Missouri's effort is typical of other states' and thus offers a good "case study".

However, the vast majority of smaller companies have shown little or no interest in international trade, especially exporting. Only ten percent of U.S. small to medium size manufacturing firms are exporting their products (12). Among these firms, fewer than one percent account for over eighty percent of small to medium size firms' exports (12).

This study solicited the opinions of 568 small firms engaged in foreign trade regarding effective ways to develop small business exports. The firms are located in Missouri, a state whose export development program features the best aspects of most state programs. These companies are Missouri exporters which employ 500 or less.

(1) The authors wish to express their appreciation to Van Psimitis of Southeast Missouri State University for obtaining the grant that made this study possible.

INTRODUCTION

Since 1970, world trade has become more important. Measured as a percent of global income, world trade grew during the 1970s and by 1982 it comprised fourteen percent of total world income (1). Data on the U.S. economy mirror an expected long-term growth in world trade (1). Imports and exports have almost doubled as a percentage of U.S. GNP since 1970 (10).

Discussions about world trade usually conjure up images of massive multinational firms. Such images are not entirely inappropriate. Multinationals control more money than the industrial reserves of all nations combined. Many multinationals have annual revenues exceeding the GNP of a substantial number of industrialized countries (3).

Prior to 1970, multinationals' dominance augured well for the United States. Firms based in the United States easily dominated world markets and thus insulated the United States domestic market from foreign competition(14). Consequently, the United States was able to continue to enjoy the luxury of not having to rely on imports in order to maintain and enhance its standard of living. Multinationals' dominance replaced other factors, namely a rapid influx of immigrants providing cheap labor, a land of rich, but untapped natural resources, and rapid development of its industrial infrastructure, which had historically prevented significant penetration of the United States domestic market by foreign competitors (14).

During the mid 1970s, however, the United States' domination of world markets began to erode. The erosion turned into a landslide in the early 1980s. Between 1982 and 1983, the deficit on the merchandise balance of trade increased from $36 billion to $61 billion (10).

Ironically, the imbalance was exacerbated by a rebound in the United States economy between 1983 and 1985. U.S. consumers' demand for imports accompanied the rise in U.S. consumers' real income. But the major U.S. trading partners recovered at a slower rate. As a result, the demand for imports of U.S. goods went down, the dollar became overvalued, and the trade deficit soared to record heights (14).

Concurrent to mounting apprehensions regarding the trade imbalance was increased appreciation of small companies' contribution to the overall soundness of the U.S. economy. The 1980 White House Conference on Small Business symbolized a revival of activity and interest (13) involving small business. Milton D. Stewart, the Small Business Administration's former chief counsel for advocacy, voiced the spirit of the meeting by calling the 1980s the "turn-around decade for small business"(7)

Enthusiasm and attention generated by the White House Conference resulted in a number of key measures designed to aid small business. One initiative was the Export Trading company (ETC) Act of 1982. Another was the provision of small business set-asides at the Export-Import Bank. A less publicized measure was an export promotion module included in recently created planning modules for Small Business Institute (SBI) Directors (4). "Free trade zones" was a fourth tool (6).

State governments have tried to complement the federal initiatives. The State of Missouri, for example, operates trade offices in Asia and Europe, provides funds for trade delegations, holds an annual Governor's Trade Conference, employs a liaison officer to coordinate and initiate state and federal efforts, pursues an aggressive campaign of telemarketing and mass mailings, and has an on-line community profile computer network database which may be accessed from any phone in the world (2).

Despite their efforts and those at the federal level, there is strong evidence that existing export development measures have proven unsuccessful. Continued growth in the trade deficit, and a persistent absence of small business involvement in export trade (14) signal problems in existing export development programs for small business.

Small firms play such a vital role in the U.S. economy that a significant rise in their export trade would produce a significant drop in the U.S. trade deficit (5). The export activities of small firms are of vital importance to the U.S. economy's future health.

This study's purpose was to identify, according to the opinions of small firms already engaged in foreign trade, the most effective ways to encourage other small firms to become active foreign traders. More specifically, this study was meant to describe and analyze those firms' views on: 1. the extent of their knowledge of international trade. 2. the importance of foreign trade to small business. 3. the most effective ways to develop small businesses' successful involvement in foreign trade.

METHODOLOGY

Subjects

The study population was of 568 Missouri firms which have no more than 500 employees, engage in export trade, and are listed in the 1986 Missouri Directory Mining, Manufacturing, Industrial Supplies. All members of the population were surveyed.

Instrumentation

The survey response form (see appendix) contained 42 items. "Open-ended" and "forced- choice" format were used.

Consent information was in the cover letter which accompanied the response form. The form was devoid of any information which could be used to ascertain a company's identity.

Procedure

An initial mailing took place during the last week of August, 1986. A follow-up mailing took place during the last week of September, 1986. After an interval of two weeks the responses were assembled and coded.

Data Analysis

Subprogram FREQUENCIES (8) in the Statistical Package for the Social Sciences (SPSS) were used to generate summary data. SPSS Subprogram CROSSTABS (9) computed measures of association on firms' backgrounds, knowledge, concerns, and opinions about effective export development measures.

RESULTS

The initial mailing produced 94 responses and the follow-up resulted in 74 additional responses for a total of 168 usable questionnaires returned. This is a response rate of 30.1 percent.

Summary data from the firms' responses are presented in the Appendix. Data for Items 1-11 show that the firms are well-established entities whose involvement with foreign trade, especially exporting, is long-standing, fairly substantial, and dispersed over a wide range of activities.

Self-ratings data for Items 12-14 reveal that the firms think they have an average level of knowledge about foreign trade. The firms also exhibit moderate concerns about foreign trade (Items 15-17) and a moderate need or desire to learn more about it (Items 18-20).

Data for Items 21-36 show that the firms think that management assistance programs and current measures to stimulate export activity are of average effectiveness. Data for Item 37 indicate that tax incentives, grants, loans, and export trade companies are rated as the best measures to stimulate export trade.

On Items 38-40 the firms indicate that they know very little about the Export Trade Company Act of 1982 but want to learn more about it.

Data on the firms initial involvement in foreign trade, and the comments on improving exporting were revealed in Items 41-42. The most prevalent response for Item 41 (how the firm became involved in foreign trade) was that the firm was contacted by a foreign firm. The second most prevalent response was that the firm became involved in foreign trade when foreign companies responded to their advertising. Other common responses included: trade shows; word of mouth; and as a result of being a subsidiary of a foreign company.

On Item 42 the most prevalent comment/ suggestion was to minimize the "red tape" and bureaucratic procedures which now plague companies involved in foreign trade. The second most prevalent response was to provide tax incentives. Other recurring responses included: reducing or removing unfair trade restrictions; working through an export trade company; and getting the dollar in line with other countries.

Inferential data from SPSS CROSSTABS Subprogram reveal a number of strong associations between five key dependent variables (Items 1-4 and 6) and the independent variables represented by Items 7-40. Regarding Item 1, data analysis reveals a strong association between the type of firm and the firms': 1. involvement with an overseas plant (Item 11). 2. self-ratings of knowledge about importing (Item 13). 3. need to learn more about importing (Item 19). 4. views on the efficacy of tax incentives (Item 27)s and bonds and trade negotiations (Items 34-35).

Data on the number of years a firm has existed (Item 2) reveal a strong association between it and the firms': 1. ratings of the effectiveness of college courses (Item 25), tax incentives and Free Trade Zones (Items 27-28), Export Trade Companies (Item 32), and bonds and trade negotiations (Items 34-35). 2. self-ratings on knowledge of the Export Trade Company Act of 1982 (Item 39).

Inferential data on the number of persons employed by the firms (Item 3) show that it is strongly associated with the firms': 1. concerns about foreign trade and importing (Items 15-16) 2. desire to learn more about importing (Item 19).

Data for Item 4, number of years a firm has engaged in foreign trade, show that it is strongly related to the firms': 1. involvement in a management contract or manufacturing plant (Items 10-11) overseas. 2. ratings of the effectiveness of college courses (Item 26), Free Trade Zones, grants, and loans (Item 28-29), and insurance subsidies (Item 33).

Computations on Item 6, percent of revenues produced by exports, reveal that it is significantly related to the firms': 1. self-ratings of their knowledge of foreign trade and import procedures (Items 12-13). 2. desire to learn more about importing (Item 19). 3. ratings of the effectiveness of workshops, seminars, and conferences, visits by trade specialists, fairs and exhibits, and direct mail brochures/ bulletins (Items 21-24). 4. ideas on the best way to stimulate export activity (Item 37).

CONCLUSIONS

Small Missouri firms engaged in foreign trade are primarily involved in exporting and want to find ways to improve their performance. Nearly 2/3 of the firms (63%) believe that the best way to encourage exporting is through financial measures like tax incentives, grants and loans. However, a sizeable number (20%) hold the opinion that legislative tools such as Free Trade Zones or the Export Trade Company are the best way to stimulate exporting.

It is particularly noteworthy to the authors that 62 percent of Missouri exporters responding had not heard of the Export Trading Company Act of 1982. It is also important to note that 70 percent of those responding wanted to learn more about the ETC Act. This is a very strong indication that the federal and State governments have not done the necessary work to inform those in the exporting business of the law, much less those firms not presently involved in exporting.

The length (Item 4) and scope (Item 6) of firms' foreign trade have a greater impact on firms' opinions about foreign trade than the impact of factors like firms' age, size, or governance (Items 1-3). Promotional efforts, the findings suggest, should be tailored to a "market segment" of firms based on some aspect of firms' involvement with foreign trade instead of factors such as size, age, or standard industrial classification.

Finally, it was revealing to note that of all the ways that firms could have become involved in foreign trade, the specific response mentioned most often was that "the firm was contacted by a foreign firm." Surely this says something about a lack of programs from the state and federal levels to "push" American companies toward exporting.

APPENDIX

Below is a reproduction of the three page questionnaire used in this study. The frequencies of responses are indicated. When the answer required was a rating on a scale, the mean, mode, and median are reported. Non-responses were eliminated by using adjusted frequencies. The response rates are based on a sample size of 168. The codes for mean, mode, and median are shown below: x = mean Mo = mode Md = median

Small Business Institute

This is a questionnaire concerning foreign trade activities, especially exporting. Please take 5 to 10 minutes of your valuable time and help us gather some information about how small business owners and managers feel about this subject. You will be contributing to a study that will be shared with state and national officials, so your opinions are very valuable.

1. My business is organized as a (check one) 2% proprietorship. 1% partnership. 97% corporation.

2. My firm has existed for ________ years. x = 39 Mo = 40 Md = 35

3. The number of persons my firm employs is _______. x = 88 Mo = 10 Md = 33

4. My firm has engaged in foreign trade _______ years. x = 22 Mo = 20 Md = 15

5. Foreign trade (imports and exports) produces ________ percent of my firm's revenues. x = 15 Mo = 1 Md = 5

6. Exports produce _______ percent of my firm's revenues. x = 12 Mo = 1 Md = 5

Is your company involved with any of the following?

7. Export Trade Company 24% Yes 76% No

8. Export Management Company 7% Yes 93% No

9. Joint venture with foreign company 14% Yes 86% No

10. Management contract with foreign country 6% Yes 94% No

11. Manufacturing plant in a foreign country 17% Yes 83% No

The next few questions ask you to use a scale from one (1) to ten (10). One (1) means "very low or not much" while ten (10) means "very high or a great deal." In the blank beside each item fill in a number between one (1) and ten (10) to represent your feeling about the matter.

12. My firm's general KNOWLEDGE of foreign trade ______. x = 5 Mo = 5 Md = 5

13. My firm's knowledge about import procedures ______. x = 4 Mo = 1 Md = 3

14. My firm's knowledge about export procedures ______. x = 5 Mo = 8 Md = 5

15. My firm's overall CONCERN about foreign trade ______. x = 6 Mo = 10 Md = 6

16. My firm's specific concern about importing ______. x = 4 Mo = 1 Md = 4

17. My firm's specific concern about exporting ______. x = 6 Mo = 10 Md = 6

18. My firm's NEED TO LEARN MORE on foreign trade ______. x = 6 Mo = 10 Md = 6

19. My firm's need to learn more about importing ______. x = 4 Mo = 1 Md = 3

20. My firm's need to learn more about exporting ______. x = 6 Mo = 10 Md = 5

Using a scale of one (1) "not effective" to ten (10) "very effective," rate the methods government agencies attempt to help firms obtain more information about foreign trade or some aspect of it. Leave the item blank if you have no opinion or knowledge of the method.

21. Workshops, Seminars, Conferences _______ x = 5 Mo = 1 Md = 5

22. Personal Visit by Trade Specialist _______ x = 5 Mo = 1 Md = 5

23. Fairs/Exhibits _______ x = 4 Mo = 1 Md = 4

24. Direct Mail Brochures/Bulletins _______ x = 4 Mo = 1 Md = 4

25. Manuals/Books _______ x = 4 Mo = 1 Md = 4

26. College Courses _______ x = 4 Mo = 1 Md = 3

Federal and state agencies use a variety of measures to stimulate export activity by small businesses. Using the same one (1) to ten (10) scale used for items 12-20, rate the effectiveness of measures that government uses to encourage firms to engage in export trade. One (1) means "very low or not much effectiveness" while ten (10) means "very high or a great deal effectiveness." Leave the item blank if you have no opinion or knowledge of the measure.

27. Tax Incentives x = 6 Mo = 10 Md = 6

28. Free Trade Zones x = 5 Mo = 1 Md = 5

29. Grants and Loans x = 5 Mo = 1 Md = 5

30. Price Supports x = 4 Mo = 1 Md = 5

31. Patent/Licenses x = 4 Mo = 1 Md = 4

32. Export Trade Company x = 5 Mo = 5 Md = 5

33. Insurance Subsidies x = 4 Mo = 1 Md = 3

34. Bonds x = 3 Mo = 1 Md = 3

35. Trade Negotiation x = 4 Mo = 1 Md = 4

36. Trade Offices x = 5 Mo = 5 Md = 5

37. Which one of the eight measures listed in items 27-36 would be the most likely to encourage your firm to either start exporting or expand your export activities?

27. 47% 32. 13% 28. 7% 33. 1% 29. 16% 34. 1% 30. 2% 35. 6% 31. 1% 36. 6%

38. Prior to its being mentioned in this survey, had you ever before heard of the Export Trading Company Act of 1982? (check one)

38% Yes 62% No

39. On a scale from one (1) "very little" to ten (10) "a great deal," rate your knowledge about the Export Trading Company Act of 1982. Place your rating in the space provided:

_____ x = 2 Mo = 1 Md = 1

40. Would you like to learn more about the Export Trading Company Act of 1982?

70% Yes 30% No

41. Briefly explain how your firm became involved in foreign trade:

____
____

42. Your comments/suggestions on how to stimulate foreign trade, especially exporting.

____
____

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PROBLEMS WOMEN FACE IN ENTREPRENEURIAL DEVELOPMENT

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ABSTRACT

The study investigated the problems women felt were of major concern in the development and operation of their business. Only female owners of small businesses were included in the study. The sample was selected from currently operating business firms.

It is recognized that certain well-known disadvantages present a strong element of vulnerability for the small business firm. These commonly accepted disadvantages include inadequate management and marketing knowledge and practices, lack of skill preparation, lack of financial depth, and a general lack of business experience. It was felt that these stated disadvantages should be considered in trying to determine the extent of their adverse effect by female business owners.

It was found that the well-known causes of vulnerability of the small business firm applies to female owners of small business yet the timely application of proper planning techniques and methods could largely reduce, if not eliminate, the most severe problem areas.

INTRODUCTION

The heavy attrition of small business during recent years has caused increasing concern during a period when the maintenance and creation of new jobs were of vital concern in our economy. It was during this period that President Reagan expressed a strong desire to "create a strong and healthy small business community."(1) Statistics reveal that more than 500,000 new small business firms are started in the United States each year. However, while many new firms start up each year, nearly one-half of them are out of business within 18 months.(2) The Small Business Administration states that over 90 percent of small business fail as a result of poor management and marketing practices.(3) Gloria Anderson states that the major reason of the alarmingly high rate of small business closure is simply a result of incompetence.(4) Many researchers have suggested that the high rate of small business mortality results from the small business owner not knowing how to properly run the business through lack of preparation and sufficient planning prior to starting the business.

Many suggestions and recommendations have been given in an effort to reduce high job loss in trying to minimize the high failure rate of small business firms with a resulting decrease in high unemployment. The high attrition rate of small business aroused the question of "how" and "why" this situation can occur today with all of the advisory services (including low or no cost seminars, courses and conferences) available to the small business owner. Previous research studies have indicated that advisory services, even though offered at low or no cost to the small business person, is used by only a small percentage of the small business owners.(5) All small business owners face many problems in opening and satisfactorily maintaining their business. The commonly stated disadvantages creating a strong element of vulnerability for the firm includes inadequate management/marketing skills and practices, lack of financial depth, and a general lack of business experience.

According to U.S. News and World Report, over 702,000 women operate their own business firms.(6) During the 1980's more than 50,000 women have annually started their own business firms which have been included in the heavy demise of small business statistics offered for this period.(7) The increasing number of female owners of small business warrants consideration of problems encountered by the female entrepreneur. Many comments of women wanting to start a business reflect particular problems with insufficient collateral needed to obtain needed credit. A reason often given for this situation has been that almost all of the financial executives authorizing loans today are male and seem to feel that women generally do not fit the business owner stereotype. Many large banks and insurance companies do not consider loans to more vulnerable small business as being sound banking policy".(8) The main concern in the area of marketing is frequently given as a general weakness in market research. Derek F. duToit, at a seminar for small business owners, stated that probably the most important determinant in business success could well be the ability to effectively perform the market research.(9) Even when appropriate market research has been carried out prior to the business start-up, the small business owner often mistakenly assumes that their market will not change. Today, buying habits change so quickly that success belongs largely to those entrepreneurs who note market change and quickly alter their line of products or services offered to keep pace.(10) If the problems facing the female small business owner are found to be unduly severe for them as a group, perhaps special remedial steps can be taken to correct such problem areas before they become fatal to their small business operation.

SURVEY

The survey sample was composed of 300 female small business owners. A random sample was drawn from two sources: first The Pink Pages, a magazine listing only the names and addresses, of small business firms having female ownership, and second, a list of women borrowers who had obtained financial assistance through business lending sources. The firms were operating businesses and had been in operation for at least several months prior to being selected as a part of the sample.

Data was collected by questionnaire which was distributed and collected by mail. The questionnaire included several types of questions, as follows: multiple choice, forced choice, open end, ranking and dichotomous. The topic could be analyzed from different perspectives as a result of the different types of questions. Each questionnaire included sixteen questions that were divided among the areas of marketing, management (including personnel), and finance. A pilot study was made in trying to locate any major questionnaire defect or bias area that might adversely effect the survey results. The survey data was collected during November and December of 1985 with an initial return rate of 35 percent 105/300 however, 17 percent were unusable leaving a return rate of 29 percent, 87/300). The SPSS statistical package was used to analyze the research data. The study was descriptive and may or may not be a sample that is truly representative of the entire population.

Limitations of Study

The population under study included only female business owners who were included in the "Pink Pages" magazine listing only female owners of small business firms in Arkansas and adjacent areas. Also, included in the study were female small business owners who had obtained financial assistance through regular business lending sources in the same area. It is realized that some female small business owners were not contacted or were not interested in being included in the magazine. It is realized that some female owners of small business either had not obtained financial assistance or had not obtained financial assistance through regular lending sources.

Survey Results

Analysis by Question

Age Started Business:

Response Age Percentage

18-25 11.2 26-35 38.2 36-45 39.3 46-55 5.6 Over 55 5.6 ----------- 100%

Over 75 percent of the respondents started their business between the ages of 26 and 45. These two age groups account for 77.5 percent of all respondents (38.2+39.3). After a woman reaches the age of 46 she is less likely to start a business.

Marital Status:

Response Marital Status Percentage

Single 16.9 married 58.4 divorced 22.5 non response 2.2 --------- 100%

Married women account for 58.4 percent of women who started business in this survey. However, 39.4 percent were unmarried with 16.9 percent single and 22.5 percent divorced. Women who are married seem to be more likely to start a business than unmarried women. With a larger percentage of women staying single, and an increase in divorced women, this last statement should change in time.

Motherhood Status:

Response Children Percentage

children, living at home 44.9 children, not living at home 32.6 no children 16.9 no response 5.6 --------- 100%

Forty-four point nine percent of women who start their own business have children not living at home. Only 16.9 percent of women responding had no children. Almost half of the women who responded had children at home with child care being a concern.

Education Response Education Percentage

less than high school graduate 6.7 high school graduate 37.1 bachelors degree 27.0 masters degree 7.9 Ph.D. 1.1 other 20.2 --------- 100%

The majority of the respondents have a high school diploma or a bachelors degree with these areas accounting for 64.1 percent of all respondents. The other response included women with some college, Juris Doctorate, Doctor of Dental Surgery and Associate degrees. Most women in this survey who enter business have some college with 56.2 percent having gone to college.

Business Income Primary Means of Support For Household

Primary Income Response Percentage Percentage

80-100% 41.6 60-79% 14.6 40-79% 13.5 20-39% 11.2 Below 20% 19.1 ---------- 100%

The largest group of respondents claim that 80-100 percent of their primary means of support comes from their small business with 41.6 percent responding. Almost 20 percent of the women stated that less than 20 percent of their income came from their small business. This survey shows that a number of women surveyed (over 30 percent) have less than 50 percent of their primary income coming from their small business.

Balance Home-Life With Business-Life

Response Balance Percentage

very difficult 3.4 somewhat difficult 39.3 somewhat easy 32.6 very easy 24.7 --------- 100%

The majority of the small business women, 57.3 percent did not experience difficulties balancing home-life with business life. However, 39.3 percent indicate that it is somewhat difficult to balance. Only a small percentage, 3.4 percent indicated that it is very difficult to balance.

Managerial Experience When Starting Business

Response Managerial Experience Percentage

none 57.3 1-3 13.5 4-6 11.2 7-10 6.7 Over 10 11.2 --------- 100%

Most women, 70.8 percent, have very little or no managerial experience when entering small business. This finding alone could lead to a higher failure rate. The category "none" accounts for 57.3 percent of the women with no managerial experience. Part of the problem is caused by past and present discrimination in the business world. Only lately have women been able to move into the work force in large numbers.

Plan/Research (Prior to the establishment of your business did you:)

Plan/ Non- Research Yes No Responses Total

formulate an overall organization plan 43.8 55.1 1.1 100

perform marketing research 16.9 79.8 3.4 100

A little over 50 percent of the women going into small business had no business plan with almost 80 percent doing no marketing research. This lack of planning is not a good sign for success.

Credit (would you say that obtaining credit for business was:)

Obtaining Response Credit Percentage

very difficult 27 somewhat difficult 30.3 somewhat easy 16.9 very easy 22.5 non-responses 3.4 ---------- 100%

Most respondents' ability to obtain credit was somewhat difficult (30.3 + 27.0 = 57.3 percent). However, a substantial portion of respondents, 39.4 percent, felt that it was somewhat to very easy to obtain credit. The ability to obtain credit is still one of the biggest problems of women starting a new small business.

Business Income Primary Means for Support For Household

Primary Income % Response %

Below 20% 20% 20-39% 11% 40-59% 13% 60-79% 14% 80-100% 41%

Balance Home-Life With Business-Life

Very Difficult 3% Somewhat Difficult 39% Somewhat Easy 33% Very Easy 25%

Managerial Experience When Starting Business

None 57% 1-3 14% 4-6 11% 7-10 7% Over 10 11%

Personnel (In regards to personnel, how do you feel about your current systems of:)

Personnel Confident Confident Inadequate Inadequate NR Total

Evaluating employees? % of Total 27 49 21 0 2 100

Pay structure? % of Total 24.7 61.8 10.1 1.1 2.2 100

Benefits for employees? % of Total 19.1 39.3 28.1 7.9 5.6 100

Seventy-six percent of small business women surveyed about their current system of employee evaluation reacted positively. The women surveyed had a very excellent degree of confidence in this area.

Payroll structure also had an excellent degree of confidence. An overall majority, 61.8 percent, said they were confident.

Concerning benefits for employees, the women surveyed were split between confident and inadequate. The area of employee benefits is the largest problem for the small business women surveyed as far as personnel problems.

Hiring/Firing (Do you find it difficult to hire and fire:)

Very Somewhat Somewhat Very H/F Difficult Difficult Easy Easy NR Total males 13.5 33.7 32.6 14.6 5.6 100.0% % of Total

females 12.4 40.4 30.3 13.5 3.4 100.0% % of Total

The small business women surveyed seem to have a harder time hiring and firing females than they did males. There was a split between the women that found it easy to hire and fire and those that had difficulty.

CONCLUSIONS

This survey included a selected sample of female owners of small business firms. It was expected to reveal the severity of problem areas confronting female owners of small business.

The survey revealed that female small business owners attributed problems to a general lack of management planning (especially noting the failure to prepare suitable plans of operation and a lack of business experience prior to entering business). A second weakness noted the respondents, feeling that they have more difficulty in hiring/firing females than in hiring/firing males. A third major weakness was in the area of marketing planning (noting a general failure to obtain and utilize market research in locating and attracting customers). A fourth problem area was that of financial planning (especially noting a felt weakness in available collateral and inability to qualify for small business loans). These four general areas were reported as significantly more important as problem areas confronting the female business owner.

The findings of this study indicate that women contemplating entering business need to develop business experience before attempting to open a business operation. Emphasis should be placed on strengthening management's ability to hire and fire employees. Research and utilization of market information was viewed as often overlooked but would be essential in contemplating a successful business operation. Also, before attempting to negotiate a small business loan, the female should consider available collateral and means of repayment. These problems pertaining to management and marketing reflect a felt need to develop a strategic operating plan before entering business. These findings can be effectively used and are essential for the successful initiation and development of any small business firm.

FOOTNOTES

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(5) Arnold Jerry L., etal, "Small Business: An Area Ripe for Practice Development", Journal of Accounting, August 1984, P78.

(6) "How Work Force is Bing Transformed", U.S. News & World Report, 92, No. 16, April 26, 1982, P53.

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10) 98th Congress, U.S. Senate, Second Session, "Women Entrepreneurs: Their Success and Business Problems," Research in Education, 1985.

PUBLIC, PRIVATE AND UNIVERSITY SUPPORT FOR INCUBATORS AND ENTERPRISE DEVELOPMENT: A COMPARATIVE ANALYSIS

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ABSTRACT

This paper reports the results of what is known about industrial incubators through a review of the literature; presents a comparative analysis of private, public, and university support for incubators and enterprise development; and suggests directions for future research.

INTRODUCTION

The purposes of this paper are threefold. The first is to compile what is known about the concept of industrial incubators from what has been published in the literature. The second is to present a comparative analysis of public, private, and university support for incubators and enterprise development. The third purpose is to suggest directions for future research.

The term "incubator," a relatively new concept, refers to providing a new business with special types of assistance during the crucial period of its initial startup. Incubators provide an "enriched" environment that can include (1) low cost, short-term leases, (2) secretarial and word processing services, (3) a support network of professional and consulting services, and (4) access to financing (Gumpert, 1985). The recent estimate of how many incubators are in the United States is 100 and this number is rapidly growing (Gumpert, 1985). A study estimated that most incubators are publicly owned and have been in existence for one year or less (Campbell, 1985).

FOUNDERS OF INCUBATORS

City, county, federal governmental agencies, chambers of commerce, private corporations, universities, and community groups are among the organizations that are founding incubators. A widely cited private corporation having incubators is Control Data, which operates 16 such centers in various locations. One of its facilities is in an old cigar factory in Charleston, South Carolina (Nelton, 1984). Two important characteristics of Control Data's incubators are that (1) they offer new businesses a place to operate at law rental costs and (2) they are viewed as a way of renovating old buildings and revitalizing depressed areas.

The Small Business Administration has been taking a role in the development of incubators by performing a networking role. In a Market Area Plan pioneered by SBA Region V, the SBA has been instrumental in founding a number of incubators (Durkin, 1984).

Broome County, New York has been a county government that has formulated an incubator (Gissy, 1984). The goals of its formulation have been to provide adequate housing for industries desiring to locate in the county and to provide technical expertise and advice to newly formulated businesses. The results of the efforts of the county in its incubating activities have not yet been published.

Rensselaer Polytechnic Institute, also in New York, is an example of a university founding an incubator (Phalon, 1983). Like the one in Broome County, its activities have included providing housing and advice. In addition, RPI has also supplied venture capital.

Private incubators are the oldest, with a median starting date of March 1983. They are followed closely by university facilities--median starting date of April 1983, and then by public facilities -- median starting date of July 1983. Private facilities generally have more tenants; their median is 21. They are followed by university facilities, with a median of 14, and public facilities, with a median of 7.8. Consequently, private facilities are much larger. Their median size is 154,000 square feet, compared to a median size of 57,5000 square feet for universities and 36,000 square feet size for public facilities (Allen, 1985).

PREVIOUS RESEARCH

There have been two previously published studies in which the characteristics of incubators were analyzed. The first is a study of the role incubator industries played in the local economy of Westfield, Mass. (Armstrong and Mullen, 1984). The study is a result of a survey of the owners of 25 small firms which have been in business for fewer than ten years, manufacture a product, and are doing business in Westfield. The results of this study indicate that these firms are not really typical of what is now being defined as incubators. None of these firms received financial assistance from government sources, most had a customer waiting when they started, and most operated under poor physical conditions. Their employees are primarily recent technical school graduates and family members. These incubators were founded to increase employment. An important recommendation of this study was that the Chamber of Commerce develop marketing and management training programs for the incubators.

Another important study of incubators was done by Allen and Rahman. They surveyed twelve Pennsylvania incubator facilities. Of these, eight had unique financing arrangements and eight incubators had provided rental space at below market rates. But, the following important consulting services were not usually provided: business tax, advertising and marketing, and computing and information services. This Allen and Rahman study provides several contributions to the understanding of incubators. The incubators in this paper are geographically dispersed, thereby minimizing unique regional characteristics. The relationships between the new business and the incubator are described in more depth. Finally, more attention is given to the organizational structural characteristics and the objectives of the incubator facility.

FINDINGS

David Allen's pillar study in which he surveyed 46 incubators and 217 tenants from throughout the county, indicated that two types of businesses were fairly represented among the private, public, and university sponsored incubators (Allen, 1985). These were light manufacturing firms with a significant new technology component and professional service firms (i.e. lawyers, accountants, management consultants, and so forth). Table 1 reveals that other types of tenants differ. For example, nearly 75 percent of public incubators contain light manufacturing tenants which is slightly over 30 percent of all tenants in public incubators. In contrast, only 4 percent of all university incubator tenants and 11 percent of all private incubator tenants are light manufacturing.

All university facilities contain research and development (R & D) firms, comprising nearly one- third of all tenants in university incubators. In comparison, R & D firms comprise only 9.5 percent of public incubator tenants and 11.5 percent of all private incubator tenants.

Two-thirds of the private incubator facilities have retail type tenants which account for nearly one-fourth of all their tenants. Again, in comparison, only 3 percent of all university tenants are retail and almost 20 percent of public incubator tenants are of the retail type.

Incubator Financial Arrangements

Sources for financing incubator land and structures are varied and include private sector and nonprofit groups; federal, state, and local governments; and foundations (Allen, 1985). Public incubators receive about one-third of their financing from private sources (loans and mortgages); nearly 30 percent from local government; and a little over 20 percent from the federal government, mostly from the Economic Development Administration (see Table 2). The private incubators receive two-thirds of their financial support from private sector sources and one-third from local governments. University incubators receive over 30 percent of their financing from state governments, about 27 percent from local governments, and approximately 18 percent from private sector groups.

Operating expenses for incubators also rely on a variety of sources (see Table 3). Rent is the primary source of covering operating expenses for both the public and private types of incubator facilities. This is followed by federal, educational, and state sources for public incubators; private sources for the private incubators. University incubators obtain their operating expenses from state and local sources, primarily with help from rental income, private, university, and nonprofit funds.

Table 4 indicates results of responses of incubator managers who were asked about their areas of greatest financial need. The first financial need was operating expenses; second, funds for expansion and upgrading; and third, funds to private capital for tenants (Allen, 1985).

Management Assistance Services

Incubators generally provide tenants with services that can be divided into the following three categories: first, logistical or physical, which includes custodial services, conference room, lunch room, and furniture rental; second, shared office support services such as clerical, word processing, receptionist, and bookkeeping; and third, management consulting services such as marketing, accounting, preparation of business plans and legal services (Allen, 1985).

Table 5 presents responses of tenants to questions concerning what services and assistance provided by the incubator facility they deemed most important to their firm's development and growth.

The photocopier was ranked first by all the tenants in the three types of incubators, i.e., 35.8 percent of private tenants, 31.5 percent of university tenants, and 22.2 percent of public tenants. Also, among the three types of incubators, shared office service and physical and logistical services ranked higher than management consulting services, although management consulting did rank fifth with tenants in the public incubator.

Usefulness of service was also rated. Interestingly, accounting services were rated fifth by tenants housed in public incubators but only 12th and 14th by tenants in university and private incubators! (Refer to Table 5).

Although Chrisman and Hoy's 1985 study of SBDC management services provided to clients of the Athens, Georgia center more general in terms of specific services provided, the findings are interesting. Table 6 indicated that 67.8 percent of the Athens Center tenants rated the management services as "good" to "vital" and only 9.3 percent rated these services as "below average" and lower and 13 percent as "average."

CONCLUSION

Small business incubator facilities sprouted in Europe following World War II and contributed to the success of a rejuvenated post World War II economy.

In 1984 there were approximately seventy-five incubators in the United States which grew to nearly 150 by the end of 1985 and are expected to surpass the one thousand mark by 1990. The development of critical guidelines for successful business incubators should evolve from ongoing research being conducted.

Directions for Future Research

The author suggest that future research concentrate on longitudinal studies to determine: --types of incubators that tend to survive in the long-run (i.e. 2-5 years) --specific tenant managerial expertise that contributes to this long-run success. --criticalness of both external and internal financing to long-run success of firms. --periodic survey of successful former incubator tenants and the role of incubator services toward this success. --an agenda for successful incubator facilities.

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TABLE 1

Composition of Tenants in Incubator Facilities

Facilities With Such Tenants Number of Tenants Public Public University Public Private Type of Tenant % N % N % N % N % Heavy Manufacturing with 4.6 1 6.7 1 22.2 2 .5 1 .4 Large New Technology Component

Heavy Manufacturing with 9.0 2 13.3 2 11.1 1 1.0 2 .6 Small New Technology Component

Light Manufacturing with 45.5 10 53.3 8 88.9 8 9.5 19 9.2 Large New Technology Component

Light Manufacturing with 72.7 16 73.3 11 55.6 5 30.8 62 11.3 Small New Technology Component

Retail and Wholesale 40.9 9 66.4 10 22.2 2 19.4 39 24.0

Professional Personal 22.7 5 33.4 5 22.2 7 3.0 6 8.2 Services

Professional Business 50.0 11 86.7 13 87.8 9 20.4 41 24.2 Services

Research and Development 45.5 10 60.0 9 100.0 3 9.5 19 11.5

Governmental Agencies 31.8 7 46.7 7 33.3 - 3.5 7 5.5

Other 9.0 2 20.0 3 - - 2.5 5 4.9

Total 22 15 9 201

TABLE 1 Continued

Number of Tenants Private University Total Type of Tenant N % N % N

Heavy Manufacturing with 2 2.1 4 .8 7 Large New Technology Component

Heavy Manufacturing with 3 .5 1 .7 6 Small New Technology Component

Light Manufacturing with 45 14.4 27 10.4 91 Large New Technology Component

Light Manufacturing with 55 3.7 7 14.2 124 Small New Technology Component

Retail and Wholesale 117 2.7 5 18.4 161

Professional Personal 40 1.6 3 5.6 49 Services

Professional Business 118 29.4 55 24.5 214 Services

Research and Development 56 35.8 67 16.2 142

Governmental Agencies 27 9.6 18 5.9 52

Other 24 - - 3.3 29

Total 487 187 100.0 875

* Allen, D. 1985. Small business incubators and enterprise development. U.S. Department of Commerce. Appendix A. Table 4.1.

TABLE 2

Financing Sources for Land and Structures*

Source Public Private University

%** Mean N %** Mean N %** Mean N Federal Government 20.6 $949,857 7 -- -- -- 9.1 $1,000,000 1

State Government 8.8 $662,333 3 -- -- -- 36.4 $1,400,000 4

Local Government 29.4 $234,148 10 33.3 $796,666 3 27.3 $1,300,000 3

Private 32.4 $514,227 11 66.7 $1,813,333 6 18.2 $675,000 2

Nonprofit/ University 5.9 $22,500 2 -- -- -- -- -- --

Other 2.9 $84,000 1 -- -- -- -- -- --

*Fourteen facilities did not provide financing information and four have acquired free space.

**Percentage of total financing amount for that column.

Allen, D. 1985. Small business incubators and enterprise development. U.S. Department of Commerce. Appendix A, Table 5.1.1.

TABLE 3

Source and Amount of Annual Funds for Operating Revenue

Public Private University Source Mean Median N Mean Median N Mean Median N

Rents $158,941 $100,000 17 $439,875 $400,000 8 $200,000 $260,000 5

State Funds $42,500 $42,500 2 $25,000 $25,000 1 $459,500 $466,000 4

Local Funds $28,000 $28,000 1 -- -- -- $400,000 $400,000 2

Federal $55,000 -- 1 -- -- -- -- -- -- Funds

Private -- -- -- $666,666 $686,000 6 $200,000 $200,000 1

University/ $50,000 $50,000 1 -- -- -- $125,000 $125,000 1 Education

Nonprofit $16,500 $12,500 4 -- -- -- $100,000 $100,000 1

Other $171,200 $100,000 5 $42,000 $42,000 1 -- -- -- Unspecified

Allen, D. 1985. Small business incubators and enterprise development. U.S. Department of Commerce. Appendix A, Table 5.1.2.

TABLE 4

Areas of Greatest Financial Need

Public Private University Funds to Cover: Rank % N* Rank % N* Rank % N*

Operating Expenses 1 63.7 14 1 27.1 4 1 44.4 4

Expansion and/or 2 36.4 8 1 27.1 4 2 33.3 3 Upgrading of Facility

Tenant Capital- 3 22.7 5 1 27.1 4 2 33.3 3 ization

Expansion and/or 4 9.1 2 4 6.6 1 4 11.1 1 Upgrading of Equipment

Consulting 4 9.1 2 -- -- -- 4 11.1 1 Services

* Based on two mentions of need; six total nonresponses.

Allen, D. 1985. Small business incubators and enterprise development. U.S. Department of Commerce. Appendix A, Table 5.1.7.

TABLE 5

Fifteen Most Important Services for Firm's Development and Ratings of Their Usefulness

Rank Percentage of Cases Public Private University Service Public Private University

1 1 1 Photocopier 22.2 35.8 31.5 1 5 8 Clerical 22.2 19.3 11.1 1 3 3 Receptionist 22.2 24.8 18.5 4 -- 7 Government Grants and Loans 20.4 -- 13.0 5 8 5 Building Security 18.5 11.9 14.8 5 10 12 Advertising and Marketing 18.5 10.1 9.3 5 14 12 Accounting 18.5 7.3 9.3 5 14 5 Preparation of Business Plans 18.5 7.3 14.8 9 -- -- Legal Services 13.0 -- -- 9 13 2 Equity and Debt Services 13.0 8.3 20.4 11 2 8 Conference Room 11.1 27.5 11.1 11 6 -- Shipping and Receiving 11.1 13.8 -- 11 -- 3 Telephone Equipment 11.1 -- 18.5 15 4 -- Work Processing 9.3 22.0 -- -- 7 -- Office Hours Answering -- 12.8 -- -- 9 -- Telex -- 11.0 -- -- 11 -- Custodial/ Maintenance -- 9.2 -- -- 11 -- Cafeteria -- 9.2 -- -- 14 12 Furniture/Equipment Rental -- 7.3 9.3 -- -- 8 Library -- -- 11.1 -- -- 8 Research and Development -- -- 11.1 11 -- 12 Computing 11.1 -- 9.3

TABLE 5 Continued

Percentage Rating Percentage Rating Usefulness High Usefulness Low Service Public Private University Public Private University Photocopier 57.1 66.3 63.6 17.9 10.2 6.8 Clerical 48.1 31.5 21.6 25.9 46.7 43.2 Receptionist 61.5 44.6 32.4 15.4 28.3 32.4 Government Grants and Loans 32.0 -- 30.0 36.0 -- 46.7 Building Security 41.9 46.9 54.3 22.6 17.3 13.0 Advertising and Marketing 21.1 20.8 25.0 52.2 41.7 41.7 Accounting 40.0 42.9 20.0 6.7 50.0 53.3 Preparation of Business Plans 30.4 33.8 25.8 39.1 48.1 35.5 Legal Services 15.4 -- -- 46.2 -- -- Equity and Debt Services 38.9 50.0

25.0 22.2 25.0 50.0 Conference Room 27.8 51.1 38.5 36.1 16.0 20.5 Shipping and Receiving 45.5 43.2 -- 22.7 16.0 -- Telephone Equipment 38.1 -- 69.2 23.8 -- 7.7 Work Processing 35.4 30.1 -- 36.4 47.3 -- Office Hours Answering -- 38.3 -- -- 47.4 -- Telex -- 28.2 -- -- 51.3 -- Custodial/ Maintenance -- 36.3 -- -- 22.0 -- Cafeteria -- 42.6 -- -- 23.5 -- Furniture/Equipment Rental -- 29.6 78.6 -- 40.8 -- Library -- -- 46.2 -- -- 11.5 Research and Development -- -- 15.8 -- -- 36.8 Computing 30.0 -- 37.0 45.0 -- 48.1

Allen, D. 1985. Small business incubators and enterprise development. U.S. Department of Commerce. Appendix A, Table 5.3.1.

TABLE 6

Evaluation of SBDC Service (Athens Center)

Total Respondents In Business Not In Business

Evaluation # % # % # %

Worthless (0) 1 1.9% 0 0% 1 4.0%

Poor (1) 4 7.4% 3 10.3% 1 4.0%

Below Average (2) 0 0% 0 0% 0 0%

Average (3) 7 13.0% 4 13.8% 3 12.0%

Good (4) 21 38.9% 11 37.9% 10 40.0%

Excellent (5) 16 29.6% 8 27.6% 8 32.0%

Vital to Success (6) 5 9.3% 3 10.3% 2 8.0%

AVERAGE RATING 4.06 4.03 4.08

No Response 1 1 0

Chrisman, J.J. & Hoy, F. 1985. The budding entrepreneur and public sector assistance: Assessing the impact of pre-venture counseling. The University of Georgia, Athens. Unpublished research paper. Table 5, 14.

SBI/SBDC COOPERATION IN THE LATE 1980'S

Fred L. Fry, Bradley University Kim Howard, Bradley University

ABSTRACT

SBI and SBDC directors were surveyed to determine the extent of cooperation between the two programs, the attitudes of each toward the other, and the perceived future of each program if federal funding is reduced or eliminated.

INTRODUCTION

It is an understatement that management assistance programs are in a state of flux during the late 1980's. As funding for the Small Business Administration continues to be in doubt, the future of the Small Business Institute and Small Business Development Centers is uncertain at best. This uncertainty will surely grow as the end of the decade and the beginning of the 1990's approach. This paper investigates the degree of current cooperation between SBI and SBDC as well as the perceived future of each.

HISTORY OF THE SBI AND THE SBDC

In order to understand the perspective of SBI and SBDC directors toward each other, it is of value to briefly trace the history of each.

The philosophy of SBI from its inception was that it is a living laboratory for students who could gain some valuable hands-on consulting experience while providing an equally valuable service to new or small businesses in the community. The directors of SBI programs were nearly always full-time faculty members who taught courses in the business curriculum. As a result, SBI directors were always conscious of the dual objectives of the SBI program: (1) increasing the practical education of business students while (2) providing management assistance to businesses.

These dual purposes became the overriding criteria for selecting SBI cases. Businesses were sometimes rejected from the SBI program not because they did not need assistance but because the students could not achieve the learning benefits from the exercise. Conversely, SBI directors sometimes had to search for businesses that were willing to work with students, sometimes even if the help provided was not critical to the livelihood of the firm. This was particularly true in schools that had a large SBI program and, hence, needed many businesses to fill the available SBI slots.

The Small Business Institute has always been funded directly by the SBA. Although the initial $250 fee was not changed for many years, a desirable feature is that the payment is made on a fixed fee basis with the only requirement being that acceptable cases must be submitted to the SBA by a given date. The use of the funds was left strictly up to the SBI directors or college administrators.

In summary, the SBI program was an easily administered program that met the dual purpose of improving student education and providing management assistance to businesses. Many of the directors have directed the program for over a decade and are strongly committed to the SBI philosophy.

The Small Business Development Center program was started several years later than the SBI program. There are at least three differences in the structure and philosophy of the SBDC compared to the SBI.

First, the SBDC's are state coordinated. That is, either a university or a state agency is the coordinator for the entire state, thereby letting SBA deal with, at most, fifty programs rather than the 500 SBI programs. SBDC directors, thus, have to work through an additional layer of bureaucracy.

A second difference between SBDC's and SBI's is that SBDC's had the single goal of helping small businesses. This focus on small business is good, particularly since SBDC's are staffed year round rather than being operated on the semester or quarter system. Thus, the entire effort of the SBDC's is small business oriented without worrying about the educational benefit or structuring the assistance around specific time frames. SBDC's are not necessarily tied directly to an academic unit of the college. Some operate through business extension, some are part of a college business research center, and some are part of the business school administrative unit.

A third difference between SBDC's and SBI's is the funding mechanism. SBI's are funded quite simply with few strings attached. SBDC'S, on the other hand, are funded through state coordinators and are expense based rather than fixed fee based. Thus, substantial amounts of time are spent in paper work insuring that funding matched expenditures each year and that local funds are available as match to the government funds.

In summarizing the development of SBDC's they have the single objective of providing management assistance year round via a state coordinated program funded by federal and sometimes additional state monies on an expense basis. Thus, both the administration and philosophies of SBDC's are consistent with SBI but they diverge on certain key elements.

THE NEED FOR NEW DIMENSIONS OF COOPERATION

With the historical perspective in mind, it is not unreasonable to expect that cooperation between SBDC's and SBI's has sometimes been excellent and sometimes been strained. As the future of the Small Business Administration remains uncertain, it is important that the relationship between SBI and SBDC be understood and improved when necessary. Even in those cases where the SBI and SBDC do work well together or where the same person directs both groups, it may be important that they work more efficiently and effectively with each doing those activities which it does best.

THE STUDY

The study reported in this paper was designed to assess the interdependence of the SBI program with other management assistance providers with particular emphasis on the interaction and cooperation between SBI and SBDC. Related to this was an assessment of which types of management assistance each is perceived to do best. Lastly, both SBI directors and SBDC directors were asked about the future of management assistance at their school if funding were eliminated for their program.

A single survey consisting of two parts was sent to 600 SBI and SBDC directors. A total of 126 were returned by the cut-off date. Eleven questions were asked in each part of the survey. SBI directors answered Part 1, SBDC directors answered Part II, and those directors who filled both positions answered both parts.

In both parts, we asked for the following information:

a. the source of clients b. the use of funds c. the cooperation and attitudes of the two units d. the future of each if funding were eliminated e. the types of projects each unit does well f. administrative information

RESULTS

Tables 1 and 2 summarize the characteristics of respondents and their programs. If one word must be used to describe the sample it is diversity. SBI programs represented were started from 1968 (before SBA was involved) to 1986. The size ranged from a low of two cases to a high of eighty-two. The average number of contracted SBI cases was 18.7 with a median of fourteen. The average actual number of cases completed was 19.9 with a median of fifteen. Over thirty percent had ten or less with just under ten percent having over thirty.

TABLE 1 RESPONDENT CHARACTERISTICS

Responses 126 SBI Directors 95 SBDC Directors 64 Joint SBI/SBDC Directors 33 SBI Directors with no SBDC program 37 SBDC Directors with no SBI program 5

TABLE 2 PROGRAM CHARACTERISTICS

Size of Programs Min. Max. Mean Median

SBI (Contracted Cases) 2 82 18.7 14 SBI (Completed Cases) 2 82 19.9 5 SBDC (Short-term Clients) 20 1000+ 298.5 199 SBDC (Long-term Clients) 2 1000+ 109.9 37

Age of Program

SBI 1 18 10 11 SBDC 1 16 5 3

In the case of SBDC'S, similar diversity was reported. SBDC's reported a start date ranging from 1970 to 1986. The number of short-term cases reported ranged from a low of twenty to over a thousand. The average number of short-term clients was just under 300 with a median of 200. Twelve SBDC's reported servicing over five hundred short-term clients with five reporting over a thousand. On the other end of the scale, fourteen serviced less than one hundred short-term clients. The average number of long-term clients was 110 with a median of thirty-seven. Although two SBDC's had served over 450 long-term clients, over half had served less than thirty-five.

SBI/SBDC Interdependence

In order to assess the interdependency of the programs with other providers, we asked directors the source of their cases. Table 3 indicates the median responses for both SBI's and SBDC'S. Again variety is the underlying characteristic. For example, less than 25% received any cases from SCORE simply because SCORE chapters do not exist near all SBI schools. Over half did not get cases from SBDC'S, reflecting the thirty-seven programs that were not co-located with SBDC'S. Responses from SBDC directors was equally difficult to interpret. It should be noted in Table 3 that the statistic presented is the median value of those that received any of their cases from the source. In the case of SCORE, for example, the true median is zero since most SBI's and SBDC's did not get any cases from SCORE. An additional comment on Table 3 is that the modal value for SBI cases received from the SBDC is 100%. That is, nine of the forty-two SBI's that use SBDC at all received all their cases from SBDC.

These statistics, while interesting, are not surprising given the nature of the two organizations and the fact that in several cases the SBI and SBDC programs are jointly administered while in others the two programs are not co-located. Where the programs are co-located, it makes sense that SBI would get many of its cases from SBDC. On the other hand and especially where the programs are not co-located, the SBI director plays a key role in the developing of SBI clients.

Similarly, given the nature of SBDC and the visibility that they attempt to maintain, one would expect that the majority of clients would come from direct contacts. It is also interesting, though to be expected given the relative size of the two programs that SBDC gets few of its clients from SBI cases not previously in contact with the SBDC.

TABLE 3 SOURCES OF CASES AND CLIENTS

SBI

SCORE 10% SBDC 40% Previous Clients 10% SBI Director efforts 60% other 25%

SBDC

SCORE 5% Previous Clients 15% SBI 5% Direct Contacts 55% Private Sources 25%

We asked SBDC directors where they refer clients to for additional assistance. Table 4 summarizes this data. Again, the statistics shown represent the median percentages for those who refer any clients to the organizations listed.

TABLE 4 SBDC CLIENT REFERRALS

SBI 5% SCORE 5% Private Consultants 10% Individual Faculty 10% Other 20%

From Table 4, perhaps the most significant fact is that most clients are handled completely by the SBDC and do not require referral elsewhere. The high number in the 'Other' probably reflects the number referred to banks, other government agencies or other organizations for specific action rather than counseling.

The conclusion from this is that SBDC's receive most of their clients from direct contacts and handle most of the cases internally. Thus, they are relatively independent of other management and SBI.

Another test of the interdependence of SBI's and SBDC's with each other and with other organizations is the amount of funds transfer between them. We asked directors how much of their funds came from or went to sources outside their own operations.

The first question asked of SBI directors was how much of the SBI funds was used beyond SBI operations such as SBDC, School of Business, or University activities. A wide variety of answers was received, but most notable was that 42% did not share any of the funds outside the SBI. Conversely, 22% reported that all of their funds went to other uses. The median response was 20% of funds being used for purposes outside the SBI.

SBDC directors were asked if they provide funds or staff to the SBI program above and beyond that funded by the SBI program itself. Surprisingly, only nine percent underwrote the SBI program at all. This suggests that SBI's are not dependent on SBDC's for funding, but they do not always have total control over the funding they do have.

SBI/SBDC ATTITUDES

Perhaps the most important part of the research dealt with the attitudes of SBI directors and SBDC directors toward each other. Both SBI and SBDC directors were asked about the cooperation between the two programs with the choices of excellent, good, fair, and poor. Table 5 shows the results. The most notable result in Table 5 is that over 20% of the SBI directors felt that cooperation was only fair or poor while 90% of the SBDC directors felt that SBI/SBDC cooperation was excellent or good. Ten percent of the SBDC directors felt that cooperation was fair and none thought it was poor. One can only speculate as to why SBI directors are less positive about the cooperativeness of SBI/SBDC relations. Even so, it should be noted that eighty percent of SBI directors and ninety percent of SBDC directors felt that cooperation was excellent or good.

Table 5 also shows results of questions that focus more on attitudes between the programs. Each director was asked their attitude of the other's program. The results are shown in the bottom of Table 5. Note again that 20% of SBI directors felt that the SBDC either was unnecessary or that it caused problems. And again, ninety-five percent of SBDC directors saw the SBI program as either an excellent counseling method or a moderate asset to the program.

TABLE 5 ATTITUDES OF SBI AND SBDC DIRECTORS TOWARD EACH OTHER

Degree of SBI SBDC Cooperation Directors Directors

Excellent 72% 78% Good 7% 12% Fair 14% 10% Poor 7% 0%

ATTITUDE OF SBI DIRECTOR TOWARD SBDC PROGRAM

The SBDC is a real asset to the SBI program 63% The SBDC has a moderate positive impact on SBI 18% The SBDC is unnecessary for SBI 18% The SBDC causes more problems than it solves 2%

ATTITUDE OF SBDC DIRECTOR TOWARD THE SBI

An excellent method of counseling 74% A moderate asset to the SBDC 21% Rather indifferent 5% A liability to management assistance 0%

ABILITY TO PERFORM

In order to get a feel for which organization would be best for which tasks, each director was asked to rank which type of projects their own operations do best. Table 6 shows this. When reading Table 6, it will be noted that there are columns for both ranking and rating the programs from 1 to 9. Some respondents interpreted the question differently than others, so results for both interpretations are presented. Although the question was not designed to create two sets of answers, those answers do shed additional light on the perceptions of the directors. This is that on a one to nine scale, no task received a median rating lower than four. Thus, both SBI and SBDC directors apparently feel that their organizations are at least somewhat capable of performing most tasks.

When looking at the rankings some similarities and some key differences appear. For example, there was agreement that Personnel, Town Studies, Computers and Business Acquisitions are among the more difficult tasks to do. This is probably because of either the magnitude or the complexity of the tasks. One key difference shows up clearly. This is in regard to business plans/loan packaging and financial analysis. SBDC directors rate these as the top two tasks that SBDC's do best. SBI'S, on the other hand, rate those two items as third and fourth with market research and accounting systems design as the top two.

TABLE 6 RANKING/RATING OF ABILITY TO PERFORM SELECTED TASKS (MEDIAN RANKING)

	SBI		SBDC	
	Ranked	Rated	Ranked	Rated
Marketing Research	2	2	4	2
Accounting Systems Design	3	3	4	2
Financial Analysis	3	3	2	2
Business Plans/Loan Packaging	3	3	2	1
Feasibility Studies	4	3	4	2
Personnel/Labor Relations	6	4	7	3
Town Studies	7	3	7	3
Computers	7	3	6	3
Acquisitions	7	5	5	3

View of the Future

The final aspect of the survey was to ascertain directors' views of the future. In particular, the interest was on the viability of each organization if federal funds were reduced or eliminated. Over forty percent of SBI directors felt that the SBI program would cease to exist at their school if federal funds were eliminated. Almost as many, however, felt that the school would underwrite it in order to keep the program. Eleven percent felt that SBI operations would be underwritten by the SBDC. When asked who would do the counseling presently done by SBI (with multiple responses allowed), forty-three percent felt that SBDC would pick up the slack, thirty-one percent felt faculty would handle it on a gratis basis, thirty-five percent felt faculty would do it on a fee basis, and fifty-five percent felt that students would continue to do it. Only fifteen percent felt that no counseling would be provided. Thus the majority felt that the counseling could be provided if SBI were eliminated.

A somewhat different opinion is voiced by the SBDC. Over half of the SBDC directors conceded that SBDC would cease to exist if federal funds were eliminated. A quarter of the respondents felt that state or local agencies would continue to underwrite the program. Less than twenty percent felt that their university or college would pick up the slack. Perhaps the most significant finding of the survey deals with the gap in counseling if SBDC's were eliminated. Whereas SBI directors indicated that someone could pick up the slack if SBI were eliminated, ninety-five percent of SBDC directors felt that there would be no one that could fill the gap in counseling left by the demise of the SBDC. This is most likely due to the size of the program and its singular focus on providing management assistance.

Historically, the philosophies of SBI and SBDC differ somewhat, primarily due to the academic focus of SBI and the longevity of the SBI program. SBDC's tend to be newer and are designed as year round sources of counseling without a necessary academic tie.

Attitudes between the two programs was generally good, although twenty percent of SBI directors rated cooperation with the SBDC as fair or poor. SBDC directors were almost uniformly positive about the SBI. This, again, may be a function of the differing philosophies of the programs, or perhaps SBI directors see SBDC as more of a threat than vice versa. SBDC directors may see SBI as a positive, but small, portion of their overall counseling portfolio.

SBI director's reported that the greatest strength of SBI lay in doing market research or accounting systems design. SBDC directors, on the other hand, saw financial analysis and business plan development as their key strength. This is a significant finding in that it offers a chance for both to improve their effectiveness as a management assistance provider by specializing somewhat in areas of greatest strength.

The one finding that is perhaps most discouraging to SBI directors even though it is not particularly surprising is that other agencies including SBDC could pick up any slack left by the demise of SBI. But, due to their size, there is no one group or combination of groups in most communities that can easily substitute for SBDC'S.

The research showed that the degree of interdependence between the two groups is not as high as might be thought. Yet, if both are to survive, cooperation will become increasingly important. Both types of directors were concerned about the end of funding with forty percent of SBI directors and over fifty percent of SBDC directors suggesting that their programs would cease to exist if funding were eliminated. This suggests strongly that the two groups should work together both to achieve internal efficiency and to pressure appropriate agencies for continuation of funding of both programs.

SCORE CONSULTATION: CLIENT PROFILE AND CLIENT'S EVALUATION

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ABSTRACT

This research is designed to identify client profile and the client's evaluation of the consulting service provided by the Service Corps of Retired Executives (SCORE). A questionnaire was mailed to 1,271 clients who came to SCORE's Chapter IV offices in the midwest region during a three month period starting December 1, 1985 and ending February 28, 1986. The questionnaire collected data regarding the client's demographics, business aspirations and characteristics, motives for seeking SCORE advice, SCORE's perceived value the client and the client's attitude towards score. The findings were analyzed according to sex and indicated that the clients were reasonably well satisfied with the service provided by SCORE and many clients were either already in business for themselves or had a viable business concept.

SCORE HISTORY

The Service Corps of Retired Executives (SCORE) is a voluntary, nonprofit organization of retired businessmen who provide consulting services to the owners of smaller business or those who wish to begin a business. These organizational objectives are accomplished through free counseling by SCORE members under the sponsorship of the U.S. Small Business Administration (SBA), however, SCORE has never been a component part of the SBA.

SCORE had its beginning in 1963, when several groups of retired men began offering free management assistance to people interested in starting a business. Later that year, the SBA began to use these volunteers in many management assistance programs. The demand for their service was very strong and encouraged them to formalize their effort by establishing local chapters. Initially, thirteen local chapters were formed and administered by the SBA. By the end of 1965, there were one hundred local chapters and SCORE counselors had advised more than 12,000 clients.

Figures from 1984 indicate that SCORE has become a viable organization with 11,800 members in 388 chapters across the country. They provided counseling to 154,000 clients, held 2,500 seminars with approximately 100,000 people in attendance.

INTRODUCTION

SCORE's history suggests a broad acceptance and high demand for the consulting services that SCORE counselors have to offer potential entrepreneurs and owners of smaller businesses. Ideally, knowledge gained by SCORE members through years of actual experience will be communicated to the client by the SCORE counselors. However, SCORE counselors have been criticized for being unfamiliar with the issues facing smaller businesses and start-up ventures; for not being familiar with the type of business that the client may have; or for being unable or unwilling to help them reach the implementation stage.

Three articles have been published (1) (2) (3) which report research findings to indicate that SCORE is not fully meeting its objectives and SCORE counselors may require additional training or SCORE may need to be reorganized in order to properly service the client.

Independent opinions of SCORE's abilities as expressed in the above mentioned articles are needed to ensure SCORE's continued vitality. But no published articles have attempted to identify the level of client satisfaction with the services being offered by SCORE nor has there been any effort to gain an insight into the client's attitude and evaluation of SCORE. Due to this lack of research, the following questions remain unanswered.

1) Who is the typical SCORE client? 2) What are the client's business aspirations? Does the typical client have a viable business concept? 3) What are the client's reason for seeking SCORE counseling? Does the client seek others for advice and if so, how does SCORE rate? 4) To what extent does the client have contact with a SCORE counselor? 5) How did the client find out about SCORE services? 6) What is the client's evaluation of SCORE? Do the clients perceive SCORE counselors as courteous? Knowledgeable? Of any benefit to them? 7) Does SCORE represent an

effective method of providing management assistance to the entrepreneur and independently owned business?

THE PROBLEM

SCORE faces an uncertain future with the pending demise or reorganization of SBA. Even though SCORE is incorporated as a non-profit 501 (c)3 organization, it still receives financial support from the SBA. In 1984, SBA had a $2.12 million budget to provide clerical support, office furnishing and supplies, communication equipment and transportation expenses for SCORE members (4). Without this support, SCORE's ability to provide free management assistance will be severely limited.

What are the alternate sources for funding SCORE? If SBA funding for SCORE is reduced or eliminated, can they pass all or part of the $2 million cost of their services on to the client? Can they find state or local public financing to support their service? Will a private source find it attractive to fund SCORE?

The first and most important first step to answering these critical questions is to determine the value of SCORE's management assistance to the client. Does SCORE have a valuable service to market? Is SCORE assisting a viable segment of the small business community? Does SCORE represent an effective method of providing management assistance to the owner and future owner of America's smaller businesses?

LITERATURE REVIEW

One problem that precipitated the need for this investigation is the lack of information which exists with regards to the clients' attitude of SCORE's consulting service. Although the sheer volume of clients that seek SCORE assistance during the year may provide a strong indication that most clients are generally satisfied, there have been no published surveys to confirm this assumption.

During the secondary research, evidence was found to indicate that some local SCORE chapters have attempted to evaluate the level of client satisfaction, however, the results were never formalized into a published report and made available for general circulation.

A computer generated literature search of the Business Periodical Index, ABI/ INFORM was able to identify only 15 articles that were published about SCORE during the twelve year period between April 1974 and 1986. These articles can be classified as follows:

1) SCORE as an opportunity for retired executives to stay active: 3 articles (5) (6) (7). 2) General description and historical information about SCORE: 3 articles (8) (9) (10). 3) SCORE as a source of management assistance to small business: 6 articles (11) (12) (13) (14) (15) (16). 4) Formal evaluation of SCORE and its members: 3 articles (1) (2) (3).

The articles in the first three classifications provide only general background and descriptive information about SCORE and case histories about either retired executives who have found fulfillment as a SCORE volunteer or case histories of clients whose business has been helped by SCORE. These topics are similar to topics which frequently appear in local and regional newspapers and business publications.

The last classification includes two articles (1) (2) written by Anderson, Elbert and Floyd and include an in-depth evaluation of SCORE and its members.

The first article titled, "Training of SCORE/ACE Counselors Attitudes and Needs," reported the findings of a survey administered to assess the training needs of SCORE and ACE counselors and assess the counselors' attitude towards this training opportunity in addition to the counselors' willingness to participate in the training sessions.

The second article (2) published by the above mentioned authors investigated the extent of SCORE/ACE involvement in the Small Business Institute program.

In both articles, the researchers were able to identify specific areas where SCORE/ACE counselors needed to improve their current level of skill or knowledge.

The authors of the third article (3) used the findings of a study performed in 1980 by the Rockville Consulting Group to evaluate SCORE. Based on this study, the researchers recommended changes in SCORE's standard operating procedures. In this article, Ambrose and Hufer expressed some of the prevailing attitudes and opinions regarding the quality of consulting provided by SCORE counselors. They stated that some volunteers lack small business expertise, have a tendency to talk rather than do, are too esoteric or are unfamiliar with the type of business for which they are assigned to consult.

All three articles provided an important insight into the operation and design of SCORE. However, all the articles included one serious flaw: none of them considered the level of client satisfaction with the existing SCORE structure, services and method of delivery. All the articles appeared to imply that the client was dissatisfied with the current quality of consulting service provided to them by SCORE--without attempting to measure the level of satisfaction.

Also, in their concluding comments, these studies did not suggest that the client will be better served if their recommendations are implemented by SCORE, although such a relationship can be assumed if the organization structure is improved.

This study is intended to contribute to filling a major void that exists in literature regarding the value of SCORE as a management assistance resource for entrepreneurs and the smaller business enterprise. It is hoped that this primary research effort will facilitate the direction of future research to determine the best form and function for SCORE.

METHODOLOGY

A three page questionnaire was mailed to 1,271 clients who came to SCORE's Chapter IV offices in the midwest during a three month period starting December 1, 1985 and ending February 28, 1986. 231 questionnaires were returned and 8 were unuseable while 80 unopened envelopes were returned as undeliverable. This represents a response rate of 18.1%. In an attempt to improve the response rate, a university logo and address was used on the cover letter, mailing and return envelopes and the questionnaire was professionally typeset.

During the research design, it was determined that the survey instrument should measure more than simply the client's positive or negative attitude towards SCORE's service. Consequently the questionnaire was designed to measure the following six characteristics:

1) Client's demographics. 2) Client's self-employment aspiration, if they plan to start a business. 3) Client's business characteristics, if they are already in business. 4) Client's reason for seeking SCORE counseling. 5) Extent of the client's contact with SCORE. 6) Client's attitude towards SCORE's services.

This study makes the following assumptions about the above characteristics:

1) Self-Employment Aspiration: This study assumes that the client is serious about their self- employment aspirations, if they have established a starting date for their business, selected a location, determined the type of business they want to enter, calculated the total amount of financing needed to start their business, identified a source of this financing, and have sufficient experience in the trade or industry.

2) Existing Business Operation: This study assumes the client has an established business enterprise if they are able to identify the start-up date for their firm, indicate the level of sales and type of business, have at least one employee and have sufficient experience in the trade or industry.

3) Extent of Client's Contact with SCORE: The extent of the client contact with SCORE is measured by determining the number of times the client had contact with a SCORE counselor, the location of their contact, the number of counselors who met with the client, the counselor's recommendations and whether the client intends to visit a SCORE counselor within the next three months.

4) Client's Attitude: This study assumes that the client's attitude can be operationalized by using the following five attitudes expressed by the client using a seven-point Likert scale:

a) Amount of time allocated for the client's visit. b) Interest and empathy shown by the counselor. c) Degree of knowledge and information provided by the counselor. d) Degree to which the client felt the counselor was able to identify and/or recommend additional sources of information and assistance. e) Client's overall rating of the SCORE's benefit to the client.

FINDINGS

The data in Table I show that 60.5% of the clients were male with an average age of 40.1 years old. Fifty-six percent had at least a college education and 60.5% were married with an average of 1.7 dependents. The female respondent represented 36.7% of the clients (2.8% did not answer this question) and is five years younger than the typical male client. Fifty-four percent of the females had at least a college diploma and 52% were married with an average of 0.7 dependents.

The most noteworthy demographic is the clients' average age. The average age for both male and female respondent is near the high end of the range that is normally considered entrepreneurial: between 20 and 40 years old (17). In addition, 64% of the male respondents are 41 or older while only half that many females respondents (32.9%) are older than 41.

The typical male client would appear to be at or beyond the range of ages that has been called a "free choice" (18) period for entrepreneurs, and these male clients may be experiencing considerable financial and family obligations.

On the other hand, the typical female client is much younger and would be less likely to share a comparable level of obligation. This agrees with research performed by Welsch and Young (19) that showed ". . . the general pattern of woman entrepreneur (to be) younger . . . (which may) be attributed to the later entry of women into entrepreneurial endeavors." Table I shows that fewer females are married and they are more likely to have no dependents or only one dependent.

However, age also has its positive implications. The older average age does indicate that the typical SCORE client may have considerable experience, maturity, financial resources and knowledge to succeed in making their new venture idea a reality or improving/expanding their current business.

BUSINESS ASPIRATION AND OWNERSHIP

The results shown in Table II provide the basic data for determining the viability of the clients' business enterprise or business aspiration. These findings highlight the fact that considerable business potential could be present among SCORE's clients, because 50.2% of all respondents currently own and operate a small business.

Fifty-five percent of all the businesses had sales in excess of $50,000 and the average start date is 1981 with 20% of the business having been established prior to 1980.

Conversely, over 141 respondents expressed an interest in starting a business. This represents 63% of the total and indicates that there is an overlap between those who want to start a business and those who currently own a business. This questionnaire was designed to allow positive responses for both possibilities and the research did not assume that the two events had to be mutually exclusive.

The findings reported in Table II.C show that 18% of all responses expressed both the interest in starting a business and ownership of an existing business. Further analysis of the data does indicate that between 8.5% and 13.0% of the respondents may have started their business in 1986 after seeing a SCORE counselor. Data reported in Table II.B and C show that 13% of those who currently own a business started their business in 1986 and 8.5% of those who expressed both a desire to start a business and indicated ownership of a business also stated that they started their business in 1986.

The coincidence of these two aspirations, the timing of their visit (between December 1985 and February 1986), along with the date of the survey administration (June 1986), all suggest that approximately 10% of SCORE clients may have sought SCORE's counseling service just prior to launching their own business enterprise. In fact, two respondents did specifically apologize for not returning the questionnaire early because they were in the middle of starting his own business when they received the questionnaire.

If future research can verify that this "last stop" consulting service is being provided by SCORE, then SCORE has an opportunity to directly contribute to the growth and development of smaller businesses within their chapter area.

For example, Chapter IV advises over 5,000 clients/yr. This would mean that SCORE has contact with over 500 entrepreneurs who have recently started or are on the verge of starting a new venture. If the 10% figure is valid at the national level, SCORE counselors would have made contact with 15,400 entrepreneurs who will be or have just started a new business enterprise.

But are the new businesses substantial? Will they be of any consequence? Do these aspirations represent viable business concepts? According to preliminary assumptions, a viable business concept is defined by the entrepreneur's or clients ability to identify or define the following six features of their proposed venture:

Positive Responses Number % a) Select a starting date 86 38.6% b) Select a location 95 42.6% c) Identify the type of business 114 51.1% d) Calculate the amount of financing 102 45.7% e) Identify the source of financing 113 50.7% f) Experience in the trade or industry 117 52.5% g) Average number of years of experience 10.8 years

The total for each individual trait is shown above, however, when the data are sorted to include only those respondents who are able to give a positive response for all the above items, the number of respondents is reduced to 50 clients or .22.4% of the total. Although reduced in number, these findings still indicate that a significant number of SCORE's clients have dedicated considerable effort to develop their venture ideas and are coming to SCORE with more than a simple and generalized wish to "be their own boss."

In addition, the magnitude and seriousness of their new business venture is also highlighted by the following data:

1) Average amount required financing exceeds $50,000. 2) A variety of financing sources have been identified by the client, rather than focusing on only one source. 3) The client's average age and years of experience in the trade indicate a mature individual who may have the necessary skills and knowledge to be successful. 4) Table II.A.1 indicates that the most frequent reason for seeking SCORE counseling was to learn how to start a business.

CURRENT BUSINESS OWNERS

Data reported in Table II.B suggest that SCORE may have an opportunity to play an important role of helping existing firms improve their current business operations or expand their businesses. A conservative estimate of the combined sales of the firms owned by SCORE clients who responded to this survey is $18,040,000 (*) and these firms accounted for the employment of 319 full-time and 164 part-time employees. If average sales and employment figures can be extrapolated for the entire Chapter IV client base, then SCORE has an opportunity to advise owners of businesses that control sales of $374 million and employ 9,620 full-time and 3,660 part- time employees in the chapter's area.

(*) see schedule A for calculation of "estimated combined sales."

These figures represent the first published estimated of SCORE's total impact on local businesses. If these figures are verified by future studies, then SCORE is in the position to be a major resource for assisting owners of smaller businesses.

In support of the hypothesis that SCORE can have a significant impact on current businesses, Table II.A.a shows that 25.9% of the reasons for the clients' visit is to seek help in improving or expanding their current business.

EXTENT OF CLIENT CONTACT WITH SCORE

Table III.A.2 shows that both female and male clients have made an average of two visits with SCORE counselors while a third of the clients (32.7%) made three or more visits. Although the vast majority of visits were made at SCORE offices (70%), the remaining contacts were made over the telephone (23.3%), at the client's place of business (1.3%) or in other situations which were not specified (5.3%).

During the contacts, SCORE counselors recommended to less than half of the clients that they attend a workshop, seminar or conference. However, among the clients who received the recommendation, over 80% either attended the event or plan to attend in the near future.

Another positive indication of SCORE's contact with the clients is that 34.1% of the clients plan to visit a SCORE counseling center again within the next three months, and 82.5% would recommend SCORE to a friend just getting started in their own business, while 64.1% of the respondents would recommend SCORE to a friend who needed to know better ways to make a profit from his or her current business.

When asked to place a dollar value on SCORE services, 143 clients (64%) responded with an average value of $38.00/hour.

Seventy-two percent of the clients did seek advice from other sources, but 62% of those clients did not find the other sources to be any more helpful than SCORE, and of those seeking advice from other sources, only 23% paid a fee which averaged 81-50/hour. The results in Table III.B.5 do show that the female client paid other consultants 35% more than the male client.

CLIENT'S ATTITUDE TOWARDS SCORE

Following is a summary of Table V which shows the client's attitude and perception of the SCORE counselor and the type and quality of service that they provided to the client.

The summary indicates that 61% of all respondents were satisfied with SCORE and 83.2% felt that the counselors gave them adequate time to discuss their business and treated them in a polite and courteous manner. However, 24.7% of the respondents did not rate SCORE services with a favorable response, and 32.8% gave SCORE less than favorable rating for its overall effectiveness followed by 29.5% who were not satisfied with SCORE's referral network.

Mean Value 7=strongly agree 1=strongly 7=strongly Characteristic measured 1=strongly disagree agree (Table V referenda) disagree 1-3 4 5-7

1. SCORE gave adequate time & 5.85 9.0% 7.9% 83.2% were polite and courteous (A)

2. SCORE showed interest and 5.14 21.1% 8.3% 69.7% empathy (B)

3. The client was generally 4.79 26.0% 11.0% 62.4% satisfied with SCORE (F)

4. SCORE's advice is reliable 4.68 22.7% 15.9% 58.5% & accurate (G)

5. SCORE provided valuable 4.64 27.4% 13.1% 57.6% information and are knowledgeable (C)

6. The printed handout information 4.59 19.3% 13.9% 59.2% was excellent (H)

7. SCORE helped me define and 4.42 32.8% 11.2% 54.1% reach may goal (E)

8. SCORE gave me good referrals (D) 4.13 29.5% 11.7% 50.5%

9. Composite rating (1) 4.75 24.7% 11.6% 61.0%

CONCLUSIONS

The following conclusions can be drawn from these research findings:

1) The typical client is older than most entrepreneurs and has considerable business experience. More than half the clients are currently running their own small business.

2) The magnitude and seriousness of the client's business aspiration have been documented by this survey. If these findings are found valid by future research, SCORE represents a major source of management assistance for the entrepreneurs and smaller business owners.

3) Clients do have extensive contact with SCORE. A significant percentage of respondents stated that they met with SCORE more than one time, followed their recommendations, and will refer friends to SCORE.

4) The most frequent way clients hear about SCORE is through friends and relatives, and this should be developed as a medium for promoting SCORE's services.

5) Even though this survey gave SCORE a generally favorable rating, SCORE should improve the following areas of their service:

a) Improve their network of referrals. b) SCORE counselors should develop their ability to help clients define their goals and identify the next step which is necessary to implement those goals. c) Counselors should improve their ability to identify the reason(s) for the client's visit. d) Improve the quality of the printed handout material. e) Counselors should continue to upgrade their skills and knowledge.

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TABLE I CLIENT PROFILE

No Respondent Characteristic Answer All Male Female No. % No. % No. % No. %

Average age: 10 4.8% less than 19 2 0.9% 1 0.1% 1 0.1% 20-25 16 7.5 10 7.3 6 7.9 26-30 36 16.9 22 16.3 14 18.4 31-35 41 19.2 22 16.3 19 25.0 36-40 29 13.6 18 13.1 11 14.5 41-45 29 13.6 19 13.9 10 13.2 46-50 16 7.5 14 10.2 2 2.6 51-55 14 6.6 11 8.0 3 4.0 56-60 20 9.4 13 9.5 7 9.1 Over 61 10 4.8 7 4.9 3 4.0

Average age: 39.6 yrs 40.1 yrs 35.4 yrs

Sex 6 2.8% 223 100% 135 60.5% 82 36.7%

Marital status 18 8.1% Married 128 57.4% 85 68.5% 41 52.0% Single 77 34.5 39 31.5 38 48.0

Education: 3 1.3% High school or less 39 17.5% 22 15.7% 17 21.3% Some college 59 26.5 39 27.9 20 25.0 College degree 60 26.9 37 26.4 23 28.8 Graduate school 62 27.8 42 30.0 20 24.9 or degree

Dependents: no dependents or no answer 105 47.1% 58 41.1% 47 58.7% 1 dependent 31 13.9 13 9.2 18 22.5 2 dependents 39 17.5 32 22.7 7 8.8 3 dependents 21 9.4 17 12.1 4 5.0 4 dependents 18 8.1 14 9.9 4 5.0 5 or More Dependents 7 4.0 7 5.0 0 0.0

Note: Unless otherwise indicated, all percentages are calculated as a percentage of the total number of respondents (223).

TABLE II CLIENT'S ASPIRATIONS

A. New Venture Creation (only positive responses)

Respondents Characteristic All Male Female No. % No. No.

1. Planning to start a bus. 141 63.2% 86 55 2. Selected a starting date 86 38.6% 56 28 3. Selected a location 95 42.6% 57 36 4. Determined type of bus. (*) a. Service for consumer 36 25.5% 19 16 b. Service for commercial and industrial clients 26 18.4 15 9 c. Authorized dealer 4 2.8 3 1 d. Wholesale business 9 6.4 7 2 e. Retail store 21 14.9 9 12 f. Manufacturer 6 4.3 6 0 g. Licensed practice 7 5.0 3 4 h. Import business 2 1.4 1 1 i. Export business 3 2.1 3 0 j. Other 27 19.2 20 7

5. Need financing 102 81.5% 71 29 6. Average amount of needed $88,390 $95,479 $75,937 financing 7. Sources of financing a. Personal funds 44 21.0% 25 19 b. Parents 10 4.8 4 6 c. Relatives 9 4.3 5 4 d. Friends 11 5.2 6 5 e. Business partner 18 8.6 13 5 f. Banks 74 35.2 45 27 g. Venture capitalist 14 6.7 9 5 h. Supplier financing 10 4.8 4 6 i. Other 20 9.4 16 10

8. Clients with previous experience in trade 117 52.5% 70 44 9. Average no. of years 10.8 yrs. 9.0 yrs. 12.2 yrs.

(*) Percentage is based on total number of respondents planning to start a business (141). (**) Total responses (210) exceed the total number of respondents for this question because each respondent could indicate more than one source.

B. Clients Already Running Business Respondents Characteristic All Male Female No. % No. No.

1. Clients owning a bus. 112 50.2% 77 32 2. Start date: 1986 29 25.9% 17 11 1985 20 17.9 13 7 1984 15 13.4 9 6 1983 12 10.7 8 4 1982 6 5.4 5 1 1981 8 7.1 5 2 1980 and before 22 19.6 20 1

3. Sales: Under $20,000 26 23.2% 11 13 $20,001 to $50,000 23 20.5 15 8 50,001 to 100,000 21 18.8 14 6 100,001 to 300,000 16 14.3 14 2 300,001 to 500,000 8 7.1 8 0 $500,000 or more 15 13.4 13 1 No answer 3 2.7

4. Type of business: Service for consumer 34 30.4% 19 17 Service for commercial 26 23.2 15 11 Authorized dealer 4 3.6 3 1 Wholesaler 9 8.0 7 2 Retail store 21 18.8 9 12 Manufacturing 6 5.4 6 0 Licensed practice 7 6.3 3 4 Import business 2 1.8 1 1 Export business 3 2.5 3 0

5. Clients with experience with a similar firm 79 70.5% 54 23 6. Average years of experience 9.5 yrs. 11.3 yrs. 6.2 yrs. 7. Number with: a. Full-time employees No employees 41 36.6% One employee 28 25.0 18 10 Two employees 13 12.5 12 2 Three employees 7 6.3 4 3 Four employees 6 5.4 4 2 Five employees 5 4.5 3 2 6-10 employees 7 6.3 7 0 11-15 employees 2 1.7 1 1 16+ employees 2 1.7 2 0 Total employees (est.) 319 265 36 b. Part-time employees No employee 56 50.0% One employee 21 18.8 18 3 Two employees 15 13.4 8 7 Three employees 5 4.5 3 2 Four employees 8 7.1 6 2 Five employees 2 1.8 1 1 6-10 employees 4 3.6 3 1 11-15 employees 0 0 0 0 16+ 1 0.8 0 1 Total employees (est.) 164 90 71

All percentages are based on the total number of respondents who own a business (112).

C. Clients Who Expressed Plans to Start a Business and Ownership of an Existing Business

Respondents Characteristic All Male Female No. % No. No. 1. Business ownership and start-up 40 17.9% 27 12 2. Business start date: 1986 19 11 7 1985 7 5 2 1984 0 0 0 1983 2 1 1 1982 2 1 1 1981 3 2 1 1980 or before 7 7 0

D. Business Aspiration, Education and Sex

1. Clients who expressed a desire to start a business All Male Female

a. High school drop-out 6 2 4 b. High school diploma 21 14 7 c. Some college 41 23 17 d. College degree 35 19 14 e. Some graduate or graduate degree 41 28 13 Total 144 64.6% 72 30

2. Clients who claimed ownership of a business. All Male Female

a. High school drop-out 7 3 3 b. High school diploma 11 5 5 c. Some college 26 21 5 d. College degree 31 23 6 e. Some graduate or graduate degree 31 20 11 Total 106 47.6% 72 30

3. Clients who claimed both ownership and a desire All Male Female

a. High school drop-out 3 2 1 b. High school diploma 4 2 2 c. Some college 8 6 2 d. College degree 12 10 2 e. Some graduate or graduate degree 13 7 6 Total 40 17.9% 27 13

All percentages in C and D are based on the total number of respondents (223).

TABLE III

A. Motive for Client Visit and Extent of Client Contact All Male Female

1. Reasons for obtaining advice from SCORE a. Learn how to start a business 118 57 58 b. Identify places to start a business 78 48 28 c. Seek help to improve current business 53 36 15 d. Seek help to expand a current business 35 24 9 e. Just followed friend's recommendation 17 10 7 f. Other reasons 39 26 13

2. Number of times the client had contact with a SCORE counselor a. only once 98 56 39 b. twice 52 33 16 c. three times 31 19 11 d. four or more times 42 25 17

3. Estimated total number of contacts 463 279 172

4. Average number of contacts/respondent 2.1 2.1 2.1

5. Clients met SCORE in the following manner: a. SCORE offices 211 126 79 b. client's place of business 4 2 2 c. over the telephone 70 46 24 d. other situations 16 11 5

6. Number of clients SCORE recommended to attend a. seminar, conference or workshop yes 103 51 50 a. if yes, number who attended yes 59 27 30 b. number who plan to attend yes 27 13 14

7. Clients Response to the Following Questions: a. Will you visit SCORE in the next 3 mos.? yes 76 41 30 no 132 87 43 no answer 15 4 10

b. Would you recommend that a friend see SCORE before starting a business? yes 184 105 73 no 38 27 10 no answer 1 1 0 c. Would you recommend that a friend see SCORE before expanding business? yes 173 100 67 no 43 29 13 no answer 7 4 3 d. Can you place a dollar value on SCORE's counseling service? yes 143 86 53 What Is the Rate Per Hour? $38 $47 $27 e. Did you seek advice from another source? yes 160 95 59 f. Were any of the other sources more helpful? yes 74 44 27 no 99 58 39 no answer 50 31 17 g. If you used another source, did you pay them a fee? yes 37 23 12 no 111 67 41 no answer 75 43 30 h. If yes, what was the rate/hour? $82 $77 $103 i. How many SCORE counselors sat with you during your last visit? only one 77 39 35 two 132 84 46 three 13 10 2

TABLE IV HOW THE CLIENT HEARD ABOUT SCORE SERVICES

All Respondents Source number percent

1. radio 21 7.8% 2. television 11 4.1 3. newspaper 34 12.6 4. friends & relatives 77 28.5 5. seminar they attended 28 10.4 6. direct mail advertising 13 4.8 7. trade association 10 3.7 8. other 76 28.1 Total 270 100.0%

Note: Respondents could indicate more than one source. Therefore the percent figure is based on the above total (270) and indicates the most-to-least frequent way clients learn about SCORE.

SCHEDULE A

Sales Category as Shown on the Estimated* Number of Estimated Questionnaire Average Sales/Firm X Firms Sales

Under $20,000 $10,000 X 26 = 260,000 20,001 to $50,000 $35,000 X 23 = 805,000 50,001 to 100,000 $75,000 X 21 = 1,575,000 100,001 to 300,000 $200,000 X 16 = 3,200,000 300,001 to 500,000 $400,000 X 8 = 3,200,000 $500,000 or more $600,000 X 15 = 9,000,000 Total Estimated Sales 18,040,000

* Assume normal distribution within each range, except the $500,000 or more category.

TABLE V CLIENT'S ATTITUDE OF SCORE

Scale Characteristics 0 1 2 3 4 5 6 7

A. Time and Patience 1. given adequate time 2 7 5 14 26 34 34 101 2. SCORE was polite & courteous 0 5 4 5 9 26 47 127 Total 2 12 9 19 35 60 81 228

B. Interest and Empathy 1. SCORE seemed genuinely interested 0 19 9 15 15 29 39 103 2. SCORE understood my problem 4 28 12 17 22 35 39 66 Total 4 44 21 29 37 64 78 169

C. Knowledge and Information 1. SCORE seemed knowledgeable 6 12 14 13 32 31 42 73 2. SCORE gave me alot of valuable info. 2 24 25 15 24 35 38 60 3. SCORE gave me information I needed 1 33 20 22 27 29 29 62 4. I will seek

SCORE advice again 8 39 15 12 34 28 18 69 Total 17 108 74 62 117 123 127 264

D. Referral Network 1. SCORE referred me to the right source 10 29 30 15 30 26 28 55 2. Rating of the referral source 28 27 10 20 22 38 26 52 Total 38 56 40 35 52 64 54 107

E. Overall Benefit to the Client 1. The session met the purpose of my visit 3 35 18 13 23 22 34 75 2. The counseling helped me reach my goal 7 37 23 20 28 25 33 50 3. SCORE helped me define my action plan 2 38 24 12 24 32 28 63 Total 12 110 65 45 75 79 95 188

F. Client Satisfaction 1. I was very satisfied with SCORE advice 3 32 28 8 20 24 37 71 2. Rating of the overall quality of SCORE 2 20 11 17 29 33 45 66 Total 5 52 39 25 49 57 82 137

G. Dependence and Accuracy 1. Advice was accurate and realistic 6 17 17 18 35 31 45 54 2. I followed SCORE's advice 7 24 14 11 36 33 41 57 Total 13 41 31 29 71 64 86 111

H. Printed Information: Total 1. Rating of the printed handout material 17 21 12 10 31 32 35 65

I. Composite Rating: Total 100 444 291 254 467 540 638 1,269

Scale: 0 = No response 1 = Strongly disagree or rating of poor 7 = Strongly agree or rating of excellent

SMALLER FIRMS AND THE EXPORT TRADING COMPANY ACT: OVERCOMING ATTITUDINAL BARRIERS TO IMPLEMENTATION

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ABSTRACT

This paper examines some of the key attitudinal factors that contribute to the reluctance of small- to medium-sized firms to utilize export trading companies for launching exporting programs and presents suggestions for overcoming or dealing with these problems. Essentially, this paper argues that the primary responsibility for more effectively penetrating foreign markets lies with the small- to medium-size business sector of the economy and the export trading company industry. The authors also suggest that the educational sector (i.e., institutions with small business institute programs) take a proactive stance in bringing smaller firms and export trading companies together.

INTRODUCTION

It is an indisputable fact that the U. S. has been losing its margin of economic leadership for more than thirty years. Reflecting this condition, trade deficits of the magnitude experienced by the United States in recent years are unprecedented. More significantly, since the mid 1960's the profitability of U. S. companies has declined, and, for the last decade, the returns on manufacturing assets have hardly been above those of corporate bonds. Loss of market shares and profitability over a sustained period are unmistakably signs of a nation's declining competitiveness (13).

As the American share of the global market has decreased, the Federal Government has been under increasing pressure to take actions designed to alleviate the problem. One response to this pressure was the passage in 1982 of the Export Trading Company Act by the U. S. Congress. This legislation was designed to encourage the formation of export trading companies (ETCS) by modifying antitrust criteria, reducing trade financing restrictions, and allowing banks and other financial institutions to become investors in such ventures.

Despite implementation of the ETC Act, the Commerce Department estimated that 30,000 small to medium sized firms are capable of exporting, but do not (11). Furthermore, the vital statistics remain basically the same:

1. About 85 percent of this country's exports can be traced to only 250 firms (14); and 2. Of the estimated 250,000 manufacturers that export goods, less than 1 percent of these firms accounts for more than 80 percent of the total export volume of this group (7).

The predictions made at the time the ETC Act was passed have failed to materialize. In fact, the U.S. trade deficit has worsened, growing from $36 billion in 1980 to $148 billion by the end of 1985 (6). The purpose of this paper is to identify some of the key factors that contribute to the reluctance on the part of small to medium sized firms to utilize export trading companies for launching or expanding exporting programs. This paper also offers suggestions for overcoming some of these problems.

BACKGROUND

The passage of the ETC Act of 1982 was a declaration by the Reagan Administration that export promotion would be a fundamental objective of the government. Congress envisioned export trading companies as a viable and innovative means to increase exports, particularly the exporting of goods by small and medium sized firms. The ETC Act's purpose was to encourage businesses to join together to export by relaxing certain antitrust regulations. Under the Act, the Commerce Secretary may authorize qualified ETCs for partial protection from antitrust statutes. This allows firms to join together for export purposes without fear of antitrust violations. The rationale underlying this provision of the law was that allowing collaboration among domestic firms for export purposes would encourage the formation of ETCS, and, therefore, the export effectiveness of these firms.

Even though this provision was thought to be conducive to exporting activities, performance has fallen far short of expectations. In reviewing the results of the ETC Act, export attorney Thomas Johnson commented that "The Act did not influence companies to start or stop trading, (but instead) those already experienced were given the additional comfort the act spelled out" (14). The lackluster ability of this legislation to seriously stimulate exporting activities among the nation's smaller and medium- sized firms can be attributed, in part, to various economic and legal factors which existed at the time of its passage. Such structural barriers include: (1) the strength of the U. S. dollar relative to other major currencies during the early 1980's; (2) the size of the U. S. domestic market which has negated the economic necessity experienced by our trading partners to engage in substantive inter-

national trade; (3) the cash poor and debt ridden condition of many of America's trading partners; (4) the magnitude of the Federal budget deficit which has resulted in significant cuts to the EX-IM Bank; and (5) the multitude of government regulations which have a significant influence upon production costs for American manufacturers.

Many of these barriers, though formidable in nature, are also quite dynamic. That is, the situation confronting domestic producers today is quite different from those in place at the time of passage and early implementation of the Act. For example, the economic climate has improved considerably within the last year for domestic firms contemplating international expansion strategies. Specifically, declines in the strength of the U. S. dollar relative to other currencies, inflation, interest rates and oil prices have all contributed to making American based producers more competitive overseas (9). These reversals will not only have the effect of driving down production and transportation costs, but will also give American producers more pricing flexibility in international markets.

Structural considerations alone, however, cannot account for the ineffectiveness of the ETC Act in stimulating increased export activity. Many researchers and practitioners also have pointed to several more subtle barriers peculiar to the smaller business sector as potential explanations for our nation's poor trade related performance. By recognizing what the underlying components of these attitudinal barriers are, both researchers and educators can then develop programs targeted at helping smaller firms overcome such resistance.

ATTITUDINAL BARRIERS

The reluctance of smaller firms to engage in more extensive international trade is quite perplexing. This situation becomes even more pronounced when one considers that the primary purpose of establishing federally authorized trading companies was to assist smaller firms in launching international strategies. Historically, however, research evidence has suggested that many smaller firms tend to view the exporting arena as the exclusive domain of large international companies. As a result, the vast majority of executives from this sector have never even considered exporting as a meaningful strategic alternative. Most prefer instead to concentrate their efforts on what they perceive to be a constantly growing domestic market (12; 15). This domestic focus, over many years, has produced a great number of smaller firms which lack any type of familiarity with doing business in foreign markets. Such a compromising position has led naturally to the development of a very cautious and conservative posture among small firms with respect to exporting (3).

Cooper (2)reported that the complex planning, organization, and product adjustments required for foreign markets also discourage many firms from attempting to extend into international markets. Clearly, perceived complexity of both the export process and international business stand as signif- icant barriers to further small business participation. Furthermore, the cost and difficulty of launching an export trading company are sizeable. Many small to medium sized firms view such endeavors as beyond their capitalization and personnel capabilities (7). Acutely concerned with profits, smaller firms have been reluctant to export because of the perceived low rate of return when compared to the risks involved. As a result, small to medium sized firms have not developed cultural understanding, language proficiency, seasoned personnel, and other skills necessary to compete overseas.

The dilemma is that ETC's are a means for overcoming many of these barriers. Surely this was the government's intention in passing the Act. ETCs may provide export related services to companies or groups of companies. These services can include, but are not limited to, market research, product promotion, sales assistance, and distribution (14). But the lack of experience of small firms in exporting and working with ETCs results in smaller firms simply deciding not to try. Until ETCs prove to be beneficial and profitable, smaller firms may continue to be hesitant to utilize an ETC. Yet without greater participation in international markets by smaller firms, ETCs will find that the opportunities to prove themselves will remain elusive.

An additional barrier to small to medium sized firm utilization of ETCs identified by the authors may be one of the most difficult to overcome. It has to do with the entrepreneurial characteristics of ten associated with the individuals who run small to medium sized firms.

Small firms are of ten innovative and responsive to change (i.e. entrepreneurial). Guiding these firms' actions are individuals of ten found to possess certain characteristics that differentiate them from the overall population. Mitton (10) noted that some key characteristics of entrepreneurs are their need for autonomy and their tendencies to position themselves so as to control the flow of information, the dispensing of rewards and punishments, and the allocation of critical resources. Entrepreneurs appear to prefer situations where their independence and achievement orientation are unbridled. They also have a high need for "outcomes" to be the result of personal efforts and not the result of influences beyond their control (15).

Although these characteristics appear to relate to firms' capabilities for innovation and responsiveness to change, they also appear to act as distinct barriers to small and medium sized firm involvement in ETC activities. Utilization of such external brokers could be interpreted by these firms as having to yield a portion of control over business operations to the exporting agent. To some extent, product acceptance and/or the reputation of the smaller firm in foreign markets would be determined by the quality and level of performance of the ETC. Since the entrepreneur prefers autonomy and control, the ETC may be perceived as incompatable with such preferences. An entrepreneur may not be willing to compromise implicitly important values for the use of an ETC, if such involvement goes against the grain of the entrepreneur.

OVERCOMING THE BARRIERS: SOME SUGGESTIONS

Overcoming the barriers to effective utilization of export trading companies will not be easy. First, the economic and political climates within which exporters and ETCs operate must be conducive to international trade activity. Second, those smaller to medium sized firms possessing export capabilities must reevaluate their inherent prejudices against exporting, in general, and the use of export trading companies, in particular. Third, export trading companies must take a more aggressive approach in positioning themselves to more adequately serve the needs of a clientele inexperienced in the global business arena.

As discussed earlier, the economic climate, with respect to the strength of the U.S. dollar, interest rates, inflation and oil prices, has improved considerably since the inception of the Act (9). From a political perspective, however, the situation with respect to the trade deficit is much more tenuous. The Federal Government presently stands at a major crossroad in developing an effective approach toward dealing with the nation's massive imbalances. Numerous special interest groups have launched substantial lobbying efforts to force Congress to enact legislation designed to protect domestic producers in home markets. Their objective is to cut the trade deficit by curtailing the level of import activity within certain industries. Contrary to this approach, the Reagan Administration has been actively resisting protectionist measures in favor of instituting a trade policy designed to open up foreign markets to American firms. Clearly, within the near future, Congress and the executive branch will be forced to come to grips with deciding how best to proceed with these delicate issues.

Changes in the economic and political climates will not in and of themselves spur export activity among small to medium sized firms to any great extent. Changes in these factors would merely provide an improved framework. What will make a difference, in combination with improved economic and political conditions, is if the major participants under consideration (i.e., the small business sector and export trading companies) each take a more proactive stance toward each other. A shared goal of helping each other to achieve greater involvement in international markets is needed.

The Small Business Sector

Recent research has shown that smaller firms which have engaged in exporting activities have experienced some degree of success. That exporting opportunities are present for smaller firms is difficult to deny (4; 5). In light of these opportunities, smaller firms with products which may be suitable for exporting need to come to grips with the fact that the real barrier to exporting is self imposed. These firms must learn to overcome the attitudinal barriers inhibiting their desire to penetrate foreign markets.

Once the top executives of smaller businesses recognize that the most important barrier to their engaging in exporting activities is their reluctance to do so, their next step should be to take a closer look at ETCS. From an understanding of what ETCs are and can do, executives of smaller firms will come to realize that ETCs are export vehicles designed to aid them in dealing with the complexities of international trade.

ETCs can operate as export merchants or export agents. As a merchant, an ETC takes title to goods and then attempts to sell these goods to foreign markets on its own account (1). This approach relieves the top executives of smaller firms of many of the responsibilities involved in exporting (except product liability) and allows them to treat the ETC as a customer similar to their other domestic clientele. When ETCs are utilized as merchants, the independence and autonomy so highly valued by entrepreneurs remain uncompromised. The small business manager need not give up control, and in return, the ETC provides the expertise so important for exporting and in such short supply in smaller firms.

As an export agent, an ETC would not take title to goods, but instead, the trading firm serves to identify foreign buyers for domestically produced goods and facilitates the flow of these goods between the two parties. Fees for such arrangements are normally derived on a commission basis.

A better understanding of ETCs will also reveal an additional benefit. Financing for exporting activities can also be facilitated by export trading companies. Considering that the ETC Act allows banks to become affiliated with trading companies and to take title to goods, such firms would be in a much better position to explore various financing options (8). Though the sponsoring banks are obligated to maintain strict credit standards at market rates of interest, they still are in a much better position to explore, with the firm's management, various, and possibly new, means of funding international expansion.

Thus, in light of improving economic and legal backdrops, and the considerable amount of flexibility available in ETC arrangements, small firms should actively begin to seek out, explore and incorporate the services of competent ETCs to aid them in designing international strategies. To aid interested firms in finding out more about exporting and ETCS, the Department of Commerce has established the Office of Export Trading Company Affairs (OETA). This agency is charged with the respon-

sibility of encouraging the formation of ETCs and to facilitate contact between producers of exportable goods and services and firms offering export services. In this capacity, the agency has published a Contact Facilitation Service Directory which lists, by state, both export service providers and U.S. producers of goods and services that wish to be registered.

Export Trading Companies

For their part, export trading companies must learn to be more responsive to the needs of their clientele. For example, Bello and Williamson (1) suggest that the type of product exported and the size of the export client have fundamental implications for service provisions. That is, in order to enhance a trading firm's effectiveness in competing in global markets, it must be able to individualize its service offerings according to such factors as foreign markets to be served and products to be sold. This would call for trading firms to adopt a global marketing mentality which would force them to rethink how they could better serve their present and potential clientele.

Research evidence also indicates that many smaller firms are unaware of the existence of ETCs (16). To deal with this situation, trading companies must place a greater emphasis on marketing their services. In the few years since the inception of the ETC Act, most trading firms were probably more concerned with establishing international networks and servicing their existing customers. Yet, in order to fuel future, more profitable growth, these companies must now focus on developing aggressive marketing campaigns which target the small business sector, a virtually untapped resource.

CONCLUSION

More than three years after the passage of the Export Trading Company Act of 1982, expectations remain largely unfulfilled. Economic, legal and attitudinal factors have acted as major barriers to small- to medium-sized firms becoming involved with ETCs. The ETC Act essentially dealt with only a small fraction of the whole problem of weak U. S. export activities, especially among small to medium sized firms.

For a change in the attitudes of the executives of smaller firms to come about, some degree of self evaluation is required. Recognition that the major barrier to smaller firm exporting is a lack of desire to do so would open up the possibility for these executives to investigate what ETCs are and what they can do. Even under present legislation, significant flexibility is available to allow accommodation and mutual benefit. Entrepreneurs can maintain their independence and enjoy the rewards exporting offers.

Export trading companies have what smaller firms require--expertise and the means to facilitate their financial requirements. But these companies need to adopt a marketing orientation not just via foreign markets, but also in their relations with potential exporters. The services an export company can provide must be sold, something ETCs have tended to ignore in the past. Executives of smaller firms need to be shown the benefits of collaborating with competitors. The belief on the part of smaller firms that exporting is too complex can be overcome by ETCs demonstrating that they can provide marketing expertise, knowledge of international business, and greater economies of scale. Accordingly, through effective deliverance of these services, ETCs would constitute a viable alternative to in house exporting activities.

Czinkota (3) suggested that intense "handholding" on the part of large, experienced exporting firms would help. What also would help is if the educational sector (i. e. institutions with small business institute programs) were to take a proactive stance in bringing smaller firms and export trading companies together. Recognizing that it takes time to achieve results, it may be possible to coax smaller firms into ETC utilization.

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A STUDY OF SBI CLIENT SATISFACTION LEVELS

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ABSTRACT

This paper reports on the results of a survey of 146 small business owners who participated in SBI projects at 13 colleges and universities in the Southern California area. The business owners were asked to evaluate the SBI program shortly after their cases were completed. Their evaluations are reviewed and analyzed, with some rather surprising results.

INTRODUCTION

During the 1985-86 academic year a total of 190 Small Business Institute (SBI) clients were sent a brief survey instrument seeking their evaluation of the just completed SBI student project. The surveys were sent to the clients between one week and two months of the completion of the SBI case. Valid survey instruments were returned by 146 small business clients, for a response rate of 76.8%.

Thirteen colleges and universities participated in the SBI program in the Southern California area. The largest participating school was UCLA, and the smallest was Westmont College in Santa Barbara (with a total of 700 students in the school). The smallest SBI contract was for six cases at Antelope Valley Junior College in Lancaster, California. The largest contract was for 60 cases at Cal State Los Angeles. Clients who worked with SBI teams from "large" schools returned 102 questionnaires (69.9% of the total respondents). "Small" school clients returned a total of 44 survey instruments (30.1%). The breakdown of the SBI schools, by size of school (large verses small), follows.

LARGE SCHOOLS

UCLA Cal State San Bernardino Cal State Dominguez Hills Cal State Fullerton Cal State Long Beach Cal State Los Angeles Cal State Northridge Cal Poly Pomona

SMALL SCHOOLS

Loyola Marymount University Antelope Valley College California Lutheran College Whittier College Westmont College

The small business firms responding to the study were categorized by type of business, as shown in Table 1 on the next page.

SBI CLIENTS RATE THE OVERALL PROGRAM

The Likert Scale survey questions were asked in an attempt to determine how the client/owners felt about the SBI program, in general, after their encounter with a student team for a school term. A ten point scale was used, with 10 equating to an "Outstanding" rating, and a 1 equating to a "Useless" rating. The responses filled the full range of options from 10 to 1. The answers to the first question can be found in Table 2 on the following page.

Based upon the high average responses shown in this table, SBI project directors could be rather smug and state that an average response rate of eight on a scale of ten is certainly quite positive. Yes, it is certainly positive, and cause for satisfaction. However, before we get too self- approving, it should be pointed out that this question has been asked of SBI clients over the past four years, and the client satisfaction level has been steadily declining, as can be noted below.

TABLE 1

SURVEY RESPONDENTS TYPE OF BUSINESS

TYPE BUSINESS	LARGE SCHOOLS		SMALL SCHOOLS		ALL SCHOOLS	
	#	%	#	%	#	%
Manufacturing	32	31.4	7	15.9	39	26.7
Retailing	29	28.4	13	29.5	42	28.8
Service	41	40.2	24	54.5	65	44.5
TOTAL	102	100.0	44	100.0	146	100.0

TABLE 2

QUESTION 1, OVERALL, HOW WOULD YOU RATE THE STUDENT CONSULTING PROGRAM?

TYPE RESPONDENT RESPONSE AVERAGE

All Respondents 8.007 Large School Clients 7.598 Small School Clients 8.955 Manufacturers 7.385 Retailers 7.929 Service Firms 8.431

TABLE 3

QUESTION ONE OVERALL RESPONSE AVERAGES

ACADEMIC YEAR OVERALL RESPONSE AVERAGE

1982-1983 8.420 1984-1985 8.145 1985-1986 8.007

One can hope that this decline is just an aberration in the figures from year to year, and does not represent a continuing trend. It is planned that this study will continue on an annual, or longitudinal basis, so that overall trends can be determined. Despite the slight decline shown over the past several years, generally speaking, all levels involved in the SBI program can take satisfaction from the fact that the SBI clients seem to have a very strong positive feeling about their encounter with a student team.

As will be noted in the responses to other questions in this survey, "Small" school clients were notably more satisfied with the SBI student team. This is a result that has shown up in previous surveys and does stir the interest of this researcher. What is the cause of this difference? Does it indicate that there is truly a difference in the quality or methods used in managing the SBI program at the larger (generally public) schools verses the smaller (usually private) schools? I cannot answer these questions based upon the research I have done with these clients, but it certainly points to a need for more in-depth research to attempt to find the causes for this difference in satisfaction levels.

In like manner, generally, throughout all of the questions in this SBI client survey, the service firms reported decidedly stronger positive feelings towards the SBI team and program than did manufacturing firms. Retail firms were also substantially more satisfied than manufacturing firms. This tendency showed up regardless of the size of school, or question asked, throughout this study. Perhaps this interesting result could be the subject of further, and more in depth research.

In the previous question we asked the SBI clients how they rated the SBI program based upon their specific encounter with their specific SBI team. A second Likert Scale question as asked, approaching this issue from a different direction. The clients were asked "Would you Recommend This Program To Other Small Business Owners?". The response options ranged from 10 (which meant "Absolutely") to 1 (which equated with a "Never" response). The results are shown in Table 4.

TABLE 4

QUESTION 2, WOULD YOU RECOMMEND THIS PROGRAM TO OTHER SMALL BUSINESS OWNERS?

TYPE RESPONDENT RESPONSE AVERAGE

All Respondents 8.342 Large School Clients 7.990 Small School Clients 9.159 Manufacturers 7.795 Retailers 8.095 Service Firms 8.831

The average response level on this question was somewhat higher than on the previous question. Perhaps some owners felt the program itself was outstanding, even though they may not have had an exceptionally good experience with their own specific team.

Once again the response levels for this question have shown a string decline since the 1982-83 school year, as shown in

Table 5, following. The clients who dealt with smaller schools and service type firms, also demonstrated the most favorable impression of the SBI Program, and were the most hearty in indicating their willingness to recommend the program to others.

In looking at the distribution of the responses to these two Likert Scale questions, roughly 75% of the responses were in the 10-9-8 range of high satisfaction. Another 20% of the responses were in the 4-5-6-7 range (classified by this writer as "fairly satisfied"). Only about 5% of the clients showed strong dissatisfaction with the SBI program by giving it a 3-2-1 rating. Using most any standard of "grading", based upon this response level, we could safely conclude that the clients have certainly rated the SBI program at approximately the "A -" level. We can be happy with that grade, but in a world that is rapidly changing around us, (Congress, the SBA, the Administration, etc.) and becoming much more critical and demanding, we must not accept anything less that a "Straight A" grade from our clients for our SBI program efforts. Thus there is still room for improvement, based upon the results of this regional research.

TABLE 5

QUESTION TWO OVERALL RESPONSE AVERAGES

ACADEMIC YEAR	OVERALL RESPONSE AVERAGE
1982-1983	8.937
1984-1985	8.382
1985-1986	8.342

SBI CLIENT REACTION TO STUDENT CONSULTANTS

In an attempt to determine how the small business owners reacted to the idea of having students work with them as consultants, two questions were asked. The first addressed the owner's overall reaction to, or satisfaction with the student team. The results appear in Table 6.

TABLE 6

QUESTION 3, HOW PLEASED WERE YOU WITH THE STUDENT TEAM?

TYPE RESPONDENT	VERY PLEASED	TEAM WAS OK	NOT PLEASED
All Respondents	70.5%	23.3%	6.2%
Large School Clients	62.8	28.4	8.8
Small School Clients	88.6	11.4	0.0
Manufacturers	64.1	28.2	7.7
Retailers	71.4	26.2	2.4
Services Firms	73.8	18.5	7.7

Once again the same patterns appear, with the small school clients showing substantially stronger satisfaction with the student counselors than large school clients. Service firms also again appear to be the most satisfied. The same result pattern holds true for Question 4 (Table 7), where the owners were asked if the students addressed the tasks they were assigned by the owners.

One might speculate at how the results would differ if these same SBI clients were asked to evaluate their pleasure and satisfaction with "adult", experienced professional consultants. Further research in this area would be of value, particularly in attempting to determine why the SBI clients appear to be so much more pleased with students from the smaller schools. One could speculate on a number of reasons for this somewhat surprising finding, but without more substantial evidence this author will refrain from personal conjecture as to the causes.

Based upon these results, overall, SBI faculty can be somewhat pleased with the client's reactions to their students. There is room for improvement, and this might be accomplished partially through an educational program where faculty and SBA personnel put forth a bit more effort aimed at getting the clients to understand that what they believe are the problems in not always what the true underlying problems turn out to be. This may partially explain the fact that about one-fifth of the clients do not believe the students fully addressed their problems. We, as SBI Directors, should also continue to monitor and direct our student's efforts to make sure that they are working on the "true" problems of the firm, and keeping their clients informed as to what they are doing, and why.

TABLE 7

QUESTION 4, DID THE STUDENTS PERFORM THEIR ASSIGNED TASK?

TYPE RESPONDENT	YES	PARTIALLY	NO
All respondents	76.0%	21.2%	2.7%
Large School Clients	67.7	28.4	3.9
Small School Clients	95.5	4.5	0.0
Manufacturers	71.8	23.1	5.1
Retailers	71.4	28.6	0.0
Service Firms	81.5	15.4	3.1

DID THE BUSINESS BENEFIT FROM SBI

The SBI clients were asked several questions to determine their level of belief that the SBI program was of value, actually benefitted their business, and was something they would be willing to be involved with in the future. The responses appear in Tables 8 - 9.

TABLE 8

QUESTION 5, HAVE YOU IMPLEMENTED THE STUDENT'S RECOMMENDATIONS?

TYPE RESPONDENT	YES	PARTIALLY	NO
All Respondents	40.4%	46.6%	13.0%
Large School Clients	29.4	53.9	16.7
Small School Clients	65.9	29.5	4.6
Manufacturers	43.6	35.9	20.5
Retailers	42.9	45.2	11.9
Service Firms	36.9	53.9	9.2

TABLE 9

QUESTION 6, DID YOUR BUSINESS BENEFIT FROM THIS PROGRAM?

TYPE RESPONDENT	YES	NO
All Respondents	87.0%	13.0%
Large School Clients	83.3	16.7
Small School Clients	95.5	4.5
Manufacturers	79.5	20.5
Retailers	83.3	16.7
Service Firms	93.8	6.2

Overall, it would appear that implementation has been less than what we might consider desirable. Before this becomes too upsetting, we must remember that these clients received these survey forms within two months of their encounter with the students, and in many cases the time span between the formal presentation of the case by the students, and the client's receipt of this survey, was substantially less than two months. Thus, often, the clients had not had time to actually implement the recommendations. In many cases the owners wrote notes along with their responses to this question stating that it was too soon to have implemented the student's suggestions. Thus we can speculate, and hope, that the level of "No" responses, regarding implementation, would diminish substantially six to twelve months after the completion of the case.

The response to Question 6 should cause SBI directors to sit up and take note! A whopping 13% of the clients said the SBI program did not benefit their business. This is a statistic that is not, and should not be, acceptable. The SBI faculty must strive for 100% "Yes" answers to this question.

Proving that our SBI programs (or all management assistant programs, for the matter) have benefited the client is critical if we are to see our SBI programs continue in their present form in future years. The SBA, Congress and the Administration will not accept our word for the value of what we do. We must also develop the ability to show, and convince, our clients that they were truly helped.

THE NEED FOR FURTHER SBI HELP

The final question of the survey asked the SBI clients if they wanted another student team to work with them. It was a surprise to this author that very close to half of the clients did want further help. This is shown in Table 10.

TABLE 10

QUESTION 7, DO YOU WANT ANOTHER STUDENT TEAM?

TYPE RESPONDENT YES NO

All Respondents 49.3% 50.7% Large School Clients 45.1 54.9 Small School Clients 59.1 40.9 Manufacturers 48.7 51.3 Retailers 42.9 57.1 Service Firms 53.8 46.2

How do we interpret this rather dramatic rate of follow-up requests? Does it mean that the team did not have enough time to finish the project fully? Could it mean that the initial team did not do too good a job, and the client wants to give it another try? Or, could it possibly mean that the client is so delighted with the program that he wants further help - perhaps with implementation? The answer is probably some combination of these choices, but considering the high levels of satisfaction shown in the answers to other questions, one could conclude that the small business owners recognize a "good deal" when they see it, and wish to "purchase" as much as possible of the SBI program to help their business.

CONCLUSION

This piece of research is recognized as a regional study, and the author recognizes that it could certainly be debated as to whether the results would fully apply nationally. It is also recognized that this is not a "heavy" piece of research, complete with a bevy of statistical formulas and significance factors and confidence levels. What it is, is an interesting study of the reactions of 146 small business owners who have participated in the SBI program. On face value their views provide some very interesting (and apparently significant) insight into client reactions to the SBI program. It should provide a basis for discussion, and in some cases definite concern and action. It can also hopefully stimulate additional research along those lines in other regions, and on a longitudinal basis, to confirm or refute these findings.

A COMPARISON OF SHOPLIFTING BEHAVIOR: DEPARTMENT STORE VS. DISCOUNT STORE

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ABSTRACT

This paper compares the shoplifting behavior of individuals who were shoplifting at a department store with those apprehended for shoplifting at a discount store. Five different variables are used for comparison purposes: the time of day the crime occurred, the method of concealment, the cost of goods stolen, the day of the week that the crime occurred, and the age of the shoplifter. A total of 354 shoplifting cases were used in this research report.

INTRODUCTION

Shoplifting is a costly crime that detrimentally affects society as well as the retailers. Estimates of annual losses attributable to the crime vary, but authorities tend to agree it is the tens of billions of dollars annually (Rogers, . 1982; National Coalition to Prevent Shoplifting, 1982; Nulty, 1980).

Consumers are affected because retailers charge a higher markup on their products in an attempt to cover the cost of pilferage. The Coalition to Prevent Shoplifting estimates that the average American family spends an additional $200 annually to cover the cost of pilferage. Society spends untold billions of dollars in law enforcement and judicial costs associated with the crime. Billions of dollars are lost to tax coffers. Besides losing billions of dollars worth of merchandise, stores are also spending increasing amounts of money to combat the problem.

Much of the shoplifting research to date have been attempts to profile the typical shoplifter (Guffey, Harris and Laumer, 1979; El-Dirghami, 1974; Boyd and Harrell, 1975; "Shoplifting Facts", 1979; Business Week, 1979; Time, 1977; Menkus, 1979; Fugate, 1980; Budden, Miller, Yeargain, 1983; Budden, 1983; Budden and Miller, 1984) and to study the economic effects of shoplifting on the economy and businesses (Faria, 1977; Business Week, 1979; Bush, 1974). Other researchers have examined the use of parental influence to prevent juvenile shoplifting (Fugate, 1980), different methods used to combat shoplifting (Faria, 1977; Menkus, 1979), and case history analyses to determine when and where shoplifting occurs (Budden, Miller and Yeargain, 1983). A review of the literature reveals a serious lack of shoplifting data as it relates to different types of retail stores. No researchers have analyzed shoplifting based on the different types of retail outlet.

RESEARCH OBJECTIVES

The purpose of this research project is to compare the shoplifting behavioral patterns that occur in department stores and discount stores. A total of five dependent variables were examined in this research project: time of day, method of concealment, cost of goods stolen, day of the week and age of the shoplifter. These variables were selected for this study based on the information gathered in the relevant literature on shoplifting. Five null hypotheses are established and tested in this research project.

H1 There is no significant difference in the time of day when shoplifting occurred in the department store and the discount store. H2 There is no significant difference in the methods used to conceal goods by the shoplifters in the department store and the discount store. H3 There is no significant difference in the cost of goods stolen between the department store and the discount store. H4 There is no significant difference in the day of the week in which shoplifting occurred at the department store and the discount store. H5 There is no significant difference in the age of the shoplifters of the department store and the discount store.

METHODOLOGY

This research project consists of an analysis of the apprehension and arrest records of a medium size department store and a discount store both located in a major southeastern SMSA. The sample consisted of all shoplifting cases that occurred over a four-year period (1978-1982) in the stores. The department store had 249 shoplifting arrests while the discount store had 105 during this time. The data were collected from the shoplifting case reports filled out by the stores' security personnel immediately after an individual had been apprehended for shoplifting.

A chi-square test was used to determine if there were significant differences in the shoplifting patterns that occurred at the department store as compared with the discount store. This nonparametric statistic was calculated using the Statistical Package for the Social Sciences. The .05 level of significance was used as a basis for rejecting the null hypothesis.

Limitations of the Study

The subjects used in this project were those actually apprehended for the crime of shoplifting. This may create a bias attributed to the fact that a majority of the shoplifters who are apprehended are amateurs as opposed to professionals. And, of course, this study does not consider those shoplifters who were not apprehended. Since the data were collected in a southeastern SMSA, one must be cautious in generalizing the findings of this research. However, the findings will be of interest in that they may form the basis for additional research and hypotheses concerning the crime of shoplifting.

Findings

Table 1 shows the data concerning shoplifting occurrences for the three time periods studied. Both stores had the same normal operating hours (9 a.m. to 9 p.m.). The day was divided into three time slots for analysis purposes: 9:00 a.m. to 1:00 p.m., 1:01 p.m. to 5:00 p.m., and 5:01 p.m. to 9:00 p.m.

Table 1

Shoplifting Occurrences Analysis Based on the Type of Store and the Time of Day

9:00 a.m. - 1:01 p.m. - 5:01 p.m. - 1:00 p.m. 5:00 p.m. 9:00 p.m.

Department Stores 46 144 58 Discount Stores 29 36 28

Chi-square = 10.920 Degrees of Freedom = 2 Significance = .0043

The null hypothesis concerning the time of day of shoplifting occurrence is rejected. The data in Table 1 indicates the major difference between the shoplifting patterns of the two stores occurs during the middle time period. The department store experienced a surge of shoplifting during this time while the discount store experienced a more uniform pattern of shoplifting.

Table 2 contains the frequencies relative to the second hypothesis which concerned the method of concealment used by the shoplifter. There were basically three methods used to conceal the merchandise. Merchandise was either hidden on the person, hidden in a purse, or hidden in a shopping bag. There were other miscellaneous methods used though no one way was predominant.

Table 2

Shoplifting Occurrences Analyzed Based on the Method of Concealment

Purse Person Bag Other

Department Stores 64 54 68 15 Discount Stores 36 40 8 18

Chi-square = 38.004 Degrees of Freedom = 3 Significance = .0001

The second hypothesis that there is no significant difference in the method of concealment is rejected. The method used to conceal the goods does vary between store types. It is interesting to note that the use of shopping bags to conceal merchandise in department stores is much more common than their use in discount stores. The people who shopped at the department store were observed carrying bags and packages more often than the customers who shopped the discount store; therefore, it was more likely that a department store shoplifter would conceal the stolen item in a bag. This can be explained by the types of products carried in the two different stores. The goods carried in a fashionable department store are traditionally classified as shopping goods; whereas, the discount store carries more goods which would fall in the classification of convenience goods. When a consumer is in the market for the purchase of shopping goods they will frequent different stores often making purchases along the way. Therefore, they are more likely to be carrying bags from one store to another. The people shopping at the discount store are often interested in making a convenience purchase, then returning home.

Store location may also play a part in this finding. The department store was located in a shopping center, and this facilitated the carrying of bags from one store to another. The discount store, on the other hand, was a free-standing store, and there would be less need for an individual to carry a bag into the store. Discount stores as a group tend to be stricter on persons carrying such bags into their stores than do department stores.

Table 3 displays the frequencies relating to the cost of the goods stolen.

Table 3

Shoplifting Occurrences Analyzed Based on the Type of Store and the Cost of the Goods Stolen

$1.00 - $20.01 - $20.00 $50.00 $50.01

Department 48 77 123 Discount 77 20 8

Chi-square = 140.009 D.F. = 2 Significance = .0001

As might be expected, the cost of the goods stolen varied significantly between the stores. Forty- nine percent of the items stolen from the department store were priced greater than $50 as compared with only 7.6% of the merchandise taken from the discount store. The relatively more expensive nature of goods in department stores as opposed to discount stores account for the difference in the value of the items taken.

Table 4 indicates the day of the week when the shoplifting apprehensions occurred. Shoplifting in the department store and discount store shows a fairly even distribution between Monday and Friday. However, there was a big increase in shoplifting on Saturday. The Chi-square test reveals that there is no significant difference between the department and discount stores based on the day of the week when shoplifting occurred.

Table 4

Shoplifting Occurrence Analysis Based on the Type of Score and the Day of the Week

Monday Tuesday Wednesday Thursday Friday Saturday

Department 36 29 45 33 38 67 Discount 12 14 14 14 18 37

Chi-square = 2.36 Degree of Freedom = 5 Significance = .7970

Null hypothesis number five states that there is no significant difference in the age of the shoplifters of the department store and the discount store. Table 5 illustrates this relationship.

Table 5

Shoplifting Occurrences Analyzed Based on the Type of Store and the Age of the Shoplifter

12-17 18-34 35-49 50+

Department 82 135 21 12 Discount 32 58 5 3

Chi-square = 1.86 Degrees of Freedom = 3 Significance = .764

The chi-square test of significance indicates that there is no significant difference between age categories and type of store.

SUMMARY

Significant differences were found on three of the five hypotheses tested. The discount store experienced shoplifting equally throughout the day while the department store had a significant rise in the crime between the hours of 1:00 and 5:00 in the afternoon. In concealing the merchandise, shoplifters working the department store tended to conceal more merchandise in shopping bags than those individuals who shoplifted at discount stores. It was noted that the department store had more expensive items shoplifted, while the discount store had relatively inexpensive items stolen.

Neither the age of the shoplifter nor the day of the week in which the shoplifting event occurred varied between the two types of retail stores. This paper is significant because it is the first attempt by any researchers to compare the shoplifting behavior of individuals who were apprehended for shoplifting at a department store with those individuals who were apprehended while shoplifting in a discount store. It is the hope of the authors that this paper will stimulate further thought and research on this important topic.

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THE MARKET OPPORTUNITY STUDY: AN SBI SERVICE TO SPUR THE DEVELOPMENT OF BLACK-OWNED BUSINESSES

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ABSTRACT

The declining state of Black-owned businesses in America is described and several theories are advanced which explain the slowdown in the establishment and growth of Black-owned businesses. As a partial solution, the author proposes conducting market opportunity studies on SBI campuses as a means of accelerating the development of Black-owned business The format for the typical market opportunity study is detailed, as well as methods for reaching potential Black entrepreneurs.

INTRODUCTION

Without a doubt, the 1980's can be characterized as the decade when the need for more Black- owned businesses became an inescapable fact. Many critics and analysts of life in Black America, including many prominent black spokespersons, have commented on the sad state of Black-owned businesses in the U.S. today. (3) Census show that Black-owned businesses lost considerable ground in both the number of firms and the sales and receipts during the period from 1977 to 1982. (1) (See Exhibit 1.)

Exhibit 1 Progress in Black Firms (1977 - 1982)

Sales # 1977 $9,504,977,000 39,968 (adjusted to 1982 dollars)

1982 $8,529,662,000 38,631

That this problem is uniquely Black is also becoming increasingly apparent. (4) During the 1970's, the numbers of new Hispanic- and Asian-owned business increased at a rate twice that of Black- owned enterprises. The gains by Asians were especially apparent in the field franchising, where, in 1973, Blacks headed more franchise restaurants than any other minority group. A disturbing reversal has taken place since that time. By 1984, Asians owned four times more franchise restaurants than did Blacks.

In southern Florida alone, Hispanics control thirty banks compared to only one by Blacks. Also, one of these Hispanic banks has assets greater than the combined assets of the nine largest Black-owned banks in the entire United States.

Added to this depressing state of affairs is the systematic, intential, and socially-accepted rebuff of many Black consumers if they conform to the typical high-crime profile: young, male, and Black. Such shoppers are either routinely denied entry to retailing establishments or discouraged from shopping by being "shooed" out of the stores. (2) These two factors: the decline in the growth of Black-owned businesses and the hostile reception of some Blacks in many mainstream retail establishments, reinforce the belief that there is a need for more Black-owned businesses especially designed to meet the needs of the Black community.

REASONS FOR SLOW GROWTH

Several theories have been advanced to explain the slowdown in the establishment and growth of Black-owned businesses over the last decade, especially when compared to the gains of other minorities.

First, Afro-American Blacks lack an entrepreneurial and/or capitalistic tradition, either from Africa or stemming from the slavery period. Instead, the Black heritage revolves around a more communitarian system which relies on familial, religious and friendship supports. This tradition is quite different from those of Asians, Hispanics and even Caribbean Blacks, all of whom have a greater familiarity with commerce. It also relates to the fact that the Black community has itself failed to lend support to Black-owned businesses. Historically, Black merchants in the Black community are held in less esteem than ministers, teachers and other establishment professionals.

Second, high crime rates in urban, Black communities discourage the establishment of small businesses. Whether from fear of robbery or the inability to hire qualified employees from the local area, the risk factor accelerates greatly when one establishes a business in this setting.

Third, the mood and the message of the present federal administration is perceived by the Black community as being "pro-white, anti-Black". The perception, then, whether justified or not, translates into an unwillingness to participate in and be part of the central economic system. Many in the Black community perceive capitalists as the enemies, the haves, the opposition. They feel that there is no place for Blacks within the capitalist system.

Last, racism still exists in America. Despite the gains of the 1950's, 1960's and 1970's, many whites still view Blacks from a distance--physically, socially and economically. They refuse to voluntarily deal with Blacks on any levels, which includes patronizing their business establishments. This may, in part, explain the growth in Asian- and Hispanic-owned businesses which has outstripped the growth in Black-owned businesses. In some instances, this willingness of some whites to accept minorities other than Blacks, has led to tension between Blacks and other minorities.

No doubt, some combination of all of the above factors has had some effect on the slowdown in Black business growth. The overall result has been that, lacking role models, incentives and inspiration, potential Black entrepreneurs languish unfulfilled. Some lack desire, others lack the funding, but too many never get started because they simply have no professional guidance in identifying business opportunities which exist in their own communities. It is in this last area that SBI programs can help. By researching, identifying and focusing attention upon the Black community, the SBI program can contribute to the development of Black-owned enterprises.

MARKET OPPORTUNITY STUDIES

The Small Business Administration is frequently confronted by clients who seek advice on starting new businesses without first having any notion of the type of businesses they wish to start. They approach the SBA seeking not only assistance on how to launch the new venture, but also in identifying what the venture will be. This is where the SBI program can be of assistance.

Small Business Institute programs, whether rural or urban, are in the unique position of being able to provide professional quality documentation on the attractiveness of ideas for new business ventures. Potential entrepreneurs in the Black community are greatly in need of such information. It is important to note that these market opportunity studies, as they might be called, can be done without first having an assigned SBI client. Instead, they can be researched from a generic standpoint, i.e. as a mechanism for describing the market and identifying problem areas which can be addressed by any interested party within the Black community.

These market opportunity studies could be assigned to university students as part of regular course assignments, in such courses as Entrepreneurism, Small Business Management and Marketing Management. The SBI director, however, is best suited to direct students in the development of market opportunity studies due to the close relationship which the director has with the Small Business Administration and the unique knowledge of the small business community which can only develop as a result of time spent working with area small businesses.

Under the director's guidance, these market opportunity reports will be able to assist potential Black entrepreneurs by serving as feasibility studies of the attractiveness of new business ideas. These reports should enable those who are considering establishing businesses in the Black community to answer many of the basic questions that need to be addressed prior to the embarkation on any business venture and to identify legitimate needs in the Black community.

Obviously, the format for the market opportunity study can vary, but the typical report should include the following:

Where? A description of the market area of interest should be readily available from census data and from observation. It should include demographic characteristics of the population, descriptions of housing, and measures of the magnitude of present commercial investment, i.e. numbers and types of retailers, wholesalers, franchises, etc.

Who? The consumer groups of interest in the market area should be identified. It is important to identify and describe the lifestyles of not only those consumer groups which have the higher levels of spending, but also those segments which display differential buying habits for whatever reason. This aspect of the research may be more dependent upon observation since such groups have been continuously ignored by the mainstream and are not referred to in readily available secondary sources. Here it is important to describe all of the consumer groups in the community, both actual and potential.

What? From the description of the consumers and the knowledge of the marketplace, unmet needs can be identified. What gaps exist between market offerings and consumer satisfaction? For example, knowledge of the number and circumstances of working and/or single parents, coupled with knowledge of local school and church facilities, combine to identify the community's need for daycare facilities. Such a focus on unmet needs could go a long way toward reversing the trend of increasing numbers of vacant store fronts in the Black community. In addition, it will help to end the perception that the only retailing establishments which are demanded in the Black community are liquor stores and bars. (2)

Competition? Once the problem has been identified, the industry of interest can be researched through universally available sources, such as Standard and Poor's. Specific competitive information within smaller geographic areas can be developed from federal government publications, such as the Census of Retailing for metropolitan statistical areas, from local government publications, and from observation.

Prerequisites for the business? Market opportunity studies should outline the necessary prerequisites for the establishment of an enterprise to meet the described need. Such prerequisites as the following can be outlined: financing, management skills, personnel requirements, and physical plant and equipment.

REACHING ENTREPRENEURS

How, then, will the contents of these market opportunity studies be relayed to potential Black entrepreneurs? Two methods are immediately apparent.

Via the SBA. The market opportunity reports can be submitted to the SBA for use in advising attendees of pre-business workshops or with any clients in need of business ideas.

Independently. Universities can conduct gratis or small fee workshops entitled "Business Idea Workshop for Black Entrepreneurs" which can be advertised in the local media. The workshops would include presentation of the market opportunity analyses as well as question-and-answer sessions for the benefit of attendees. Students could assist in the workshops by answering the questions of potential entrepreneurs. Such workshops should be successful, especially when they are publicized and promoted by the SBA.

It is realistic to expect college students to be able to develop such market opportunity studies. Many schools already engage in the development of such reports as part of course requirements. However, the unique aspect of this proposed program direction is that for the first time such studies will concentrate on the needs of the Black community and the needs of its future entrepreneurs. Those needs have never been greater than now. By the institution of such market opportunity studies, the SBI can assist in stemming the losses being experienced by Black businesses in the United States today.

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MARKET SHARE FORECASTING USING CENSUS DATA: AN INTEGRATED SPREADSHEET APPROACH

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ABSTRACT

A small business must be equipped with current and reliable information in order to provide effective guidance for its management. Marketing information is basic to effective leadership in any intensely competitive economy, and this information has to be based on facts: facts about consumers, facts about the conditions affecting the purchase, and facts about potential sales of its products. Even the most successful small business cannot afford to ignore marketing statistics as a tool for market evaluation. One important aspect of a market evaluation is estimating a markets sales potential. This paper will present a methodology in which a small business manager can conduct his own market share analysis. Specifically, he will be able to estimate the total market sales volume which exists for his business, and in addition, relate that to the sales volume which may exist in the future.

Marketing Decision Variables and Market Potential

The market for a product or service is the demand or potential demand for it which is usually expressed quantitatively by types of consumers. Therefore, markets for consumer goods consist of people who have the desire and who have the buying power to express their wants in terms of effective demand.

Generally, market potential is the expected total sales of a product, group of products, or a service in a market during a specific period of time. On the other hand, sales potential is the share of the market potential expected by an individual company.

The knowledge of potentials is essential to many marketing decisions. Planning for marketing activities begins with a careful consideration of the market and sales potentials, in as much as the basic information formulated in analyzing potential markets are utilized in the planning process. Based on these two types of potentials, the small business manager is able to develop plans as to expansion possibilities, inventory scheduling, hiring needs, and advertising planning, to mention a few.

To measure the size of a market, then, two basic types of statistics are required. First, the size of the population must be analyzed on the basis of individuals or households. Not only does the analyst need to estimate the number of people and households, but also to acquire statistics on total, average, and per capita income which will provide the analyst with an index of purchasing ability.

As the steps in the market share forecast are developed, the procedure will be illustrated with an example so you will have an understanding of the environment of a typical problem, and the typical sources of statistical data used will be identified.

Illustrative Example (Taken from an SBI Case)

Central Auto Parts is a successful family-owned and operated corporation specializing in a complete line of automotive parts for all foreign cars and some domestic small cars. The business is separated into wholesaling and retailing divisions. The wholesale warehouse is located in downtown Orlando. From there, sales are made to local retail auto parts stores, garages, and service stations. In addition to the local sales, the warehouse does a considerable mail order business to customers throughout Florida and in many other states. The retail store is located in Winter Park with population of 30,000. The growth and financial success of the business is attributed to the stability of technical and managerial strength of Mr. Jones, Sr. The firm has management manpower available through John Jones and Steve Jones, Jr. , both of whom have been involved with the business since an early age.

In 1981, sales growth was offset by increasing inflation. At the same time, profit was "just holding its own" in the retail division. This plateau caused the owner to take a hard look at his strategy for future growth. It was determined that priority be given to expanding sales at the retail level, capturing a greater, more profitable share of the do-it-yourself market in the greater Orlando metropolitan area. A new retail branch is being considered, and the owner wants to make this store as profitable as possible as soon as possible. Specifically, the goal for the new store is for it to reach a sufficient level of sales to cover all expenses in about nine months. The owner wants to know if the location selected is a feasible one in light of his objectives. He plans to open the new store in 1986.

Measure Geographical Market Size and Shape

The first step in determining the potential sales for an area is to define the area. Since auto parts are generally classified as shopping goods, people will expend some effort to obtain these goods, and they will travel approximately 15 minutes to reach the store. The market area is, therefore, approximately defined by the area within a 15-minute drive from the store location.

How can one measure an area 15 minutes in size? The most reliable way is to convert the time factor into a distance factor by taking a car trip through the area in question and noting the distance traveled within the 15 minute time allocation. So Mr. Jones, with map in hand, starting at the location he was interested in traveled in his car as far as he could within the 15 minute time limit. He then noted on the map how far he had traveled by placing a dot at that location. He then went back to the starting point and took another road from the starting location and traveled once again for 15 minutes in this new direction. He repeated this procedure until he had covered the major roads leading to and from his proposed location.

Map Out The Market Area

Back in the comfort of his home that night, he proceeded to connect the dots on the street map. He had developed what is called a "time contour" which is an area within the set time limit. In Mr. Jones case, a 15 minute limit produced a rough market area. His next task was to convert the market area from the street map to a census tract map. The reason for this step is the fact that the census tract is generally regarded as the basic unit for demographic statistics. Therefore, it is used by many government authorities in updating their estimates of population and income for a geographical area. Since a wealth of information is usually available for census tracts, we will have the market area delineated correspond to the shape of the census tract units. By simplifying this procedure in this manner it will make gathering the appropriate information much easier. However, if minor variations exist between your market area and the census tract boundaries, you should increase your market area to conform to the census tracts. If there is a large variation between the two components, you will have to readjust the proportion which lies outside your market area by taking a percentage of that census tract.

If you cannot locate census tract information for your market area, your local government may have a department of planning, a department of economic development, or some department or entity that maintains demographic information in the form of analysis zones for your area. This statistical information may take the place of census tracts.

Mr. Jones proceeded to convert the information from his market area map to the census tract map. This resulted in 14 census tracts being included for subsequent analysis.

At this point, you have a geographical shape of a market area in terms of census tracts. If the area has been carefully defined, on the basis of your time contour analysis, selective perceptions, and other information available to you, you should have a fairly good representation of an area which possibly possesses economic strength to support an enterprise.

Estimate The Population In Your Area

Having proceeded this far with your analysis, you have identified a specific geographical area as a potential source for a market for your products. The question now is, how big is the market? You want to know the size of the market in terms of the purchasing power of individuals who are likely to spend dollars in your type of business.

However, at this stage of analysis the clerical work required to answer such a question becomes a formidable task in assembling the necessary information into a presentable format for computations. To help facilitate and simplify the procedure, the author has developed an integrated spreadsheet template for Lotus 1-2-3 or VP Planner. (See the Appendix for a print out of the cells and formula set up.)

To begin to answer this question we must first estimate the population within the target market area. Mr. Jones was able to obtain 1970 and 1980 population data from the local planning council. Exhibit 1 shows a portion of the spreadsheet with the population figures for the years in question.

Since Mr. Jones is considering an opening sometime in 1986, this will be his target year which will be the year his market analysis will be based upon. If you have projected statistics for that target year, no adjustments have to be made with the data. However, if your statistics are for a year other than your target year, then you will have to adjust these data so they will represent your target year.

Since we obtained population data for each of the census tracts, we projected the population for the target year for each tract and then summed across the tracts. The calculations for each of the tracts would be as follows:

LATEST YEAR POPULATION LESS POPULATION FROM PREVIOUS DATA EQUALS TOTAL CHANGE DIVIDED BY THE # OF YEARS BETWEEN DATES EQUALS THE POPULATION CHANGE PER YEAR TIMES NUMBER OF YEARS TO TARGET YEAR ADD TO LATEST YEAR POPULATION FIGURE EQUALS POP. PROJECTED TO TARGET YEAR

DATA TO BE ENTERED INTO SPREADSHEET

Projected year: Latest year: Earliest year:

and for each census tract

Population for the latest year: Population for the earliest year:

OUTPUT

Forecast of target year population

Forecast of Total Personal Income

The next step is to estimate total personal income for the target area. Data on the income levels of the residents of the target market area should be available from the same office where you obtained your population data. If they do not have such data, they are knowledgeable concerning alternative sources. It is optimal that you obtain income data for your target year; however, this may not be available. In such cases it will be necessary to project the income levels for your target year. Therefore, you should obtain data for two different years, such as 1970 and 1980. Chances are that the income data you are seeking will be more difficult to obtain than the population information was, and you may have to take what you can get to work with. If you have a choice, however, data expressed as per capita income is what you need. If income levels are for families are the only statistics available, then use them as a second choice. And third, if income statistics are reported for households, you will have no choice but to accept them for analysis purposes.

If your income statistics are provided for your target year, you already have the necessary per capita income figures. No further projections are required. However, if you have per capita income figures for years other than your target year, you will once again have to project those figures to your target year. In our case, since the data are for households we are first going to have to convert the data into per capita figures. The general formula for this step would be as follows:

NUMBER OF HOUSEHOLDS IN CENSUS TRACTS TIMES THE MEAN HOUSEHOLD INCOME EQUALS TOTAL PERSONAL INCOME DIVIDED BY THE POPULATION EQUALS PER CAPITA INCOME

Before the final calculations in projecting income can be completed, it is necessary to convert the raw per capita income figures into constant dollars. Constant dollars is a measure of the real increase in the value of an item over a time period with the effects of inflation removed. The reason for this step is so that the real change in income trends can be separate from the effects of inflation. You will have to inflate the values you have to reflect the equivalent purchasing power for the present year. To accomplish this we can use the Consumer Price Index (CPI) which is a general indicator of inflation for consumer goods and services sold throughout the country. The CPI is estimated on a monthly basis by the U.S. Bureau of Labor Statistics, and is published in the Survey of Current Business. The CPI for

1986 (at the time of this writing it is the average of the first eight months) was 326.

The conversion calculation is not complex and is as follows: 1986 CPI DIVIDED BY 1980 (or whatever year) CPI EQUALS 1980-1986 CONVERSION FACTOR TIMES 1980 PER CAPITA INCOME

EQUALS 1980 PER CAPITA INCOME EXPRESSED IN 1986 CONSTANT DOLLARS Since we have per capita income figures available for years other than Mr. Jones's target year, we will have to project, per capita income to the target year 1986.

The following calculations illustrate the procedure:

MOST RECENT YEAR (1980) LESS A PREVIOUS YEAR (1970) EQUALS TOTAL ESTIMATED CHANGE DIVIDED BY THE NUMBER OF YEARS BETWEEN DATES EQUALS THE RATE OF CHARGE PER YEAR TIMES # OF YRS. FROM EST. TO TARGET YR EQUALS TOTAL CHANGE TO TARGET YEAR ADD CHANGE TO LAST ESTIMATE EQUALS PROJECTED PER CAP. INC. FOR TARGET YR.

Once the income is converted to current dollars, the step in determining the total personal income is a relatively simple one. It is necessary to multiply the number of people (population) by the income per person (per capita income). For Mr. Jones's case this would be: EST. MKT. AREA POP. * PER CAPITA INCOME = TOTAL PERSONAL INCOME

The procedures for calculating the total personal income for the target market is shown in Exhibit 2.

DATA TO BE ENTERED INTO SPREADSHEET Present year CPI: Latest year CPI: Earliest year CPI:

and for each census tract

Number of households latest year Mean income latest year

Number of households earliest year Mean income latest year

OUTPUT

Total personal income to target date.

Forecasting Market Share For Target Year

This stage of the analysis entails several steps. First, we need to estimate potential sales for all businesses of your type. In Mr. Jones' case it would be all establishments capable of carrying auto parts and accessories. To accomplish this you have to calculate the percentage of total personal income which is likely to be spent in your type of business. The result of this calculation is what is referred to as an "expenditure factor". To ascertain what this percentage is, it will be necessary to acquire information from additional sources. The first type of information you will need is cited in the Survey of Current Business, available at most libraries. This publication makes estimates of total personal income for each Standard Metropolitan Statistical Area (SMSA) and county throughout the United States. What you should be looking for is the total personal income for your entire SMSA for the latest year. If your considered location is outside of an SMSA, then you should use the data for your county. Another source you may want to use is the Survey of Buying Power issue published each year by Sales & Marketing Management magazine. They publish data for metro areas and this is a good surrogate.

The second type of information needed is the total sales by your type business for your geographical area. This type of data can be located in the following publications: The Census of Retail Trade, or the companion series, Census of Selected Service Industries. You will be especially interested in the "geographic area series," which includes a separate report for each state. A companion series, "major retail centers," is also available. Within the geographic area series are listed the total retail sales for each SMSA, and for each county. These data are listed by the store types and Standard Industrial Classification (SIC) code. You should select your type of business which most closely corresponds to the type of business name and SIC code from the report. If data are not reported for your particular type of business, use the next broader category from the report. Another source you may want to consider using is the Survey of Buying

Power, a publication available at most libraries. For certain selected retail types they publish sales figures by store group for Metro areas. Once again this will serve as an adequate surrogate.

At this point, then, you will have the total personal income for your SMSA (or county, or metro area) and the total sales reported for your type of business for the same SMSA (or county, or metro area) for the same year. For Mr. Jones"s case, to determine the portion of income spent on auto parts, the 1977 Census of Retail Trade for Florida was consulted to obtain the total sales for the tire, battery, and accessory dealers for auto and home supply stores in Orlando, Florida SMSA (SIC Code 553).

Using the State Metro Area Data Book (1979), again the 1970 to 1976 change in income for the Orlando SMSA was found to average an annual increase of 13 percent, so the 1976 value for income was increased 13 percent to arrive at the 1977 personal income figure for the Orlando SMSA.

To calculate the expenditure factor for your business type, we simply divide the sales figure by the total personal income figure. This will produce a decimal fraction which, after moving the decimal point two places to the right, may be expressed as a percentage. However, the decimal fraction is your expenditure factor used in the next step.

DATA TO BE ENTERED INTO SPREADSHEET

Total SMSA income: Total SMSA sales for your product:

OUTPUT

Expenditure factor =

To determine the market potential for your type of business in your market area, it is necessary to multiply the expenditure factor by the total personal income for your market area as of your target year. The result is an estimate of the total sales that are likely to occur in businesses of your type which can be supported by your market area. In other words, this figure is an estimate of sales for all businesses of your type which includes your business and all your competitors which serve your market area.

OUTPUT

This figure is calculated by the computer from the information supplied earlier in the analysis.

Remember, this figure represents an estimate of sales for ALL autoparts dealers for Mr. Jones' market area, including his competitors serving his market area. Mr. Jones' next question would be: What proportion of this amount can I expect to capture?

The series of calculations which you have just completed has yielded an estimate of the total sales generated by your type of businesses in your market area. The final step in our calculations is to determine how much of this total your business will be expected to capture. To estimate your potential market share you will have to identify your competition. This is not always an easy task, for there are many business that fall into "type or group" stores that may not directly compete with your business. For example, in Mr. Jones' case, a gas station may not really compete with his type of establishment. However, in the recording of the sales data for auto supply dealers, a computation of ALL types of auto supply and accessory places would be entered into one category entitled auto supply. For Mr. Jones' case, the overall market size we estimated would be for ALL auto parts and accessories. Therefore, one must realize that the analysis will contain establishments which may not directly compete against your type of business.

With this information, Mr. Jones now has to locate all businesses which fall under the label "auto parts and supplies". He could have accomplished this task when he developed his "time contours by noting his competition as he drove through his market area. However, he could have missed some of his competitors by not traveling on a particular street. For this reason it is recommended that you obtain directories of businesses which would include your type of business. These directories may be obtained from local Chambers of Commerce. Another source of information that can be used is the "Yellow Pages" of the telephone directory. From this publication you will be able to determine the number of competitors within your market area. At this point it is important to realize that you should look beyond your market area boundary for your competition. The reason is that establishments just beyond your boundary will still draw heavily from within your market area. Therefore, you should consider establishments just beyond your market area. It has been suggested that you should use a time-distance factor of half of what you use in delineating your market area. For example, if your time-distance factor is 15 minutes, then you should adjust your search for competition to include an area of approximately 23 minutes travel time from your business. In fact, it may be a good idea to put on your area map you developed pins representing your competition so you will have a visual picture of where they are located. Once you have obtained the number of competitors in your area, you will divide the estimated income spent on your product by the number of competitors to arrive at an estimate of your market share potential. In Mr. Jones case, he identified 27 competitors in his and adjoining market areas. He would then divide the number of competitors into the estimated amount spent for his type of product in his target area.

DATA TO BE ENTERED INTO SPREADSHEET

Enter number of competitors in your target market:

OUTPUT

Fair market share in target year is:

This does NOT necessarily mean that his share of the market will be this final figure - rather, it indicates what a FAIR share of the market may be. That is, the amount if each competitor had an equal share of the market. This figure can be adjusted for the strength or weakness of the individual's business.

CONCLUSION

The analysis you can perform using the methodology presented with the accompanying spreadsheet template can provide you with a sophisticated forecasting technique of market share potential. The microcomputer and the spreadsheet have taken all of the drudgery out of a complicated analysis. The spreadsheet enables you to quickly create a model of a situation by entering labels, numbers, and formulas. Using the program's built-in functions, you can perform complicated calculations. You can then use the completed model to explore what-if questions. If you change any variable - for instance, population, or income projections - the model will recalculate a new result automatically and instantly.

The spreadsheet model can be saved and used again whenever you need it. Never again will you forget how a specific analysis was done and have to reconstruct it from scratch the next time you need to use it. You can modify this model so that it may be used in other situations in which you need more census tracts (by adding rows) or it can grow in power (by adding columns to take into account portions of census tracts in the analysis). This model allows you to approach forecasting market share potential logically because it makes it possible to focus on the problem, not on the calculations.

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EXHIBIT 1

MARKET SHARE POTENTIAL FORECASTING SPREADSHEET FILE NAME: MKTSHARE

DATA INPUT TABLE: --------------------------- PROJECTED YEAR: 1986 LATEST YEAR: 1980 EARLIEST YEAR: 1970

ESTIMATE OF MARKET AREA POPULATION -- # OF CENSUS ANALYSIS POPULATION POPULATION TARGET YR ZONE LATEST YR EARLIEST YR POPULATION 1 5888 2967 7641 2 4531 2329 5852 3 2509 670 3612 4 4097 913 6007 5 2947 551 4385 6 1360 1089 1523 7 4063 2216 5171 8 7025 1085 10589 9 1065 1021 1091 10 4965 4729 5107 11 402 323 449 12 6785 6499 6957 13 3117 2711 3361 14 2543 652 3678 -------- --------- ------------ 51297 27755 65422.2 =========== EXHIBIT 2 PROJECTION OF PER CAPITA INCOME AND CALCULATION OF TOTAL INCOME

PRESENT YEAR CPI: 326 LATEST YEAR CPI: 247.6 EARLIEST YEAR CPI: 116.3

HOUSE- MEAN PER CAPITA HOLDS INCOME INCOME TRACT LATEST LATEST LATEST NUMBER YEAR YEAR YEAR 1 1435 25957 6326 2 1830 22924 9259 3 277 44275 4888 4 465 29634 3363 5 302 34432 3528 6 529 37120 14439 7 994 30479 7457 8 353 29414 1478 9 964 22768 20609 10 1986 27893 11157 11 1076 28465 76190 12 2455 32964 11927 13 1671 23233 12455 14 1045 17575 7222

HOUSE- MEAN PER CAPITA TOTAL HOLDS INCOME INCOME PERSONAL EARLIEST EARLIEST EARLIEST INCOME TO YEAR YEAR YEAR TARGET DATE

1011 8957 3052 48335347 937 6924 2786 54186071 195 23175 6745 17650192 328 9134 3281 20202369 213 12432 4806 15465728 373 16020 5487 21986372 700 11479 3626 38559311 249 9414 2160 15648365 476 6468 3015 22503633 1399 8393 2483 56979996 124 8465 3250 34294465 1729 11964 3183 82977411 825 8233 2505 41862015 243 5575 2078 26562314 -------------- TOTAL INCOME: 497213589 ==============

EXHIBIT 3

ENTER FOR SMSA:

TOTAL SMSA INCOME: 3942570000 TOTAL SMSA SALES: 34466000

ENTER NUMBER OF COMPETITORS IN YOUR TARGET MARKET: 27

EXPENDITURE FACTOR = .0087

TOTAL ESTIMATED SALES FOR TARGET AREA: $4,346,647.88

FAIR MARKET SHARE IN TARGET YEAR IS: $160,986.96 ==============

APPENDIX

CELL AND FORMULA SET UP FOR SPREADSHEET

A1'MARKET SHARE POTENTIAL FORECASTING SPREADSHEET A2'FILE NAME: MKTSHARE A4'DATA INPUT TABLE: A5'---------------------------- A6'PROJECTED YEAR: A7'LATEST YEAR: A8'EARLIEST YEAR: A10'ESTIMATE OF MARKET AREA POPULATION A11'--- A12'NUMBER OF CENSUS A13'TRACT, ANALYSIS ZONE A14\--- -- A15' 1 A16' 2 A17' 3 A18' 4 A19' 5 A20' 6 A21' 7 A22' 8 A23' 9 A24' 10 A25' 11 A26' 12 A27' 13 A28' 14 A34' ==================================

A36'PROJECTION OF PER CAPITA INCOME AND CALCULATION OF TOTAL INCOME A37 \ ------------------- -------------------------------- A38'PRESENT YEAR CPI: A39'LATEST YEAR CPI: A40'EARLIEST YEAR CPI: A43 \ -- A45"TRACT NUMBER A47 A48 1 A49 2 A50 3 A51 4 A52 5 A53 6 A54 7 A55 8 A56 9 A57 10 A58 11 A59 12 A60 13 A61 14 A64 \ ===========================

A66'ENTER FOR SMSA A68'TOTAL SMSA INCOME A69'TOTAL SMSA SALES: A71'ENTER NUMBER OF A72'ENTER NUMBER OF A73'TARGET MARKET: A75'EXPENDITURE FACTOR= A77'TOTAL ESTIMATED A78'SALES FOR TARGET A79'AREA: A81'FAIR MARKET SHARE A82'IN TARGET YEAR IS: B4(F2)

B6 1986 B7 1980 B8 1970 B12"POPULATION B13"LATEST YEAR B14 \ ---------------------------------- B15 5888 B16 4531 B17 2509 B18 4097 B19 2947 B20 1360 B21 4063 B22 7025 B23 1065 B24 4965 B25 402 B26 6785 B27 3117 B28 2543 B29"------- B30 @SUM(B15..B28) B34'============== B37 \ --------------------- B38 326 B39 247.6 B40 116.3 B43 \ ---------------------

B45"HOUSEHOLDS B46"LATEST YEAR B47 \ --------------------- B48 1435 B49 1830 B50 277 B51 465 B52 302 B53 529 B54 994 B55 353 B56 964 B57 1986 B58 1074 B59 2455 B60 1671 B61 1045 B64 \ =============

B68 3942570000 B69 34466000 B73 27

B75(B4) +B69/B68 B79(J2) +J63*B75 B82(B2) +B79/B73 B83" ==============

C12"POPULATION C13"EARLIEST YEAR C14 \ ----------------------- C15 2967 C16 2329 C17 670 C18 913 C19 551 C20 1089 C21 2216 C22 1085 C23 1021 C24 4729 C25 323 C26 6499 C27 2711 C28 652 C29"------- C30 @SUM (C15..C28) C34'===============

C37\----------------------------- C43\----------------------------- C45"MEAN INCOME C46"LATEST YEAR C47\-----------

------------------ C48 25957 C49 22924 C50 44275 C51 29634 C52 34432 C53 37120 C54 30479 C55 29414 C56 22768 C57 27893 C58 28465 C59 32964 C60 23233 C61 17575

D12"TARGET YEAR D13"POPULATION D14 \ ----------------------------- D15(B0) (B15-C15) / (B7-B8) * (B6-b7) + (B15) D16(B0) (B16-C16) / (B7-B8) * (B6-b7) + (B16) D17(B0) (B17-C17) / (B7-B8) * (B6-b7) + (B17) D18(B0) (B18-C18) / (B7-B8) * (B6-b7) + (B18) D19(B0) (B19-C19) / (B7-B8) * (B6-b7) + (B19) D20(B0) (B20-C20) / (B7-B8) * (B6-b7) + (B20) D21(B0) (B21-C21) / (B7-B8) * (B6-b7) + (B21) D22(B0) (B22-C22) / (B7-B8) * (B6-b7) + (B22) D23(B0) (B23-C23) / (B7-B8) * (B6-b7) + (B23) D24(B0) (B24-C24) / (B7-B8) * (B6-b7) + (B24) D25(B0) (B25-C25) / (B7-B8) * (B6-b7) + (B25) D26(B0) (B26-C26) / (B7-B8) * (B6-b7) + (B26) D27(B0) (B27-C27) / (B7-B8) * (B6-b7) + (B27) D28(B0) (B28-C28) / (B7-B8) * (B6-b7) + (B28) D29"--------- D30 @SUM(D15..D28) D31:---------- ----------

D34"==================

D43 \ ------------------------------

D45"PER CAPITA INCOME D46:LATEST YEAR D47 \ ------------------------------ D48 (B0) (B48*C48) /B15 D49 (B0) (B49*C49) /B16 D50 (B0) (B50*C50) /B17 D51 (B0) (B51*C51) /B18 D52 (B0) (B52*C52) /B19 D53 (B0) (B53*C53) /B20 D54 (B0) (B54*C54) /B21 D55 (B0) (B55*C55) /B22 D56 (B0) (B56*C56) /B23 D57 (B0) (B57*C57) /B24 D58 (B0) (B58*C58) /B25 D59 (B0) (B59*C59) /B26 D60 (B0) (B60*C60) /B27 D61 (B0) (B61*C61) /B28

E43 \ ---------------------- E44 E45^: E46^: E47 \ ---------------------- E48^: E48^: E50^: E51^: E52^: E53^: E54^: E55^: E56^: E57^: E58^: E59^: E60^: E61^: F43 \ ------------------------ F44 F45"HOUSEHOLDS F46"EARLIEST YEAR F47 \ ------------------------ F48 1011 F49 937 F50 195 F51 328 F52 213 F53 373 F54 700 F55 249 F56 467 F57 1399 F58 124 F59 1729 F60 825 F61 243 G43 \ ----------------------- G44 G45"MEAN INCOME G46"EARLIEST YEAR G47 \ ----------------------- G48 8957 G49 6924 G50 23175 G51 9134 G52 12432 G53 16020 G54 11432 G55 9414 G56 6468 G57 8393 G58 8465 G59 11964 G60 8233 G61 5575

H43 \ ----------------------- H44 H45"PER CAPITA INCOME H46"EARLIEST YEAR H47 \ ----------------------- H48 (F0) (F48*G48) /C15 H49 (F0) (F49*G49) /C16 H50 (F0) (F50*G50) /C17 H51 (F0) (F51*G51) /C18 H52 (F0) (F52*G52) /C19 H53 (F0) (F53*G53) /C20 H54 (F0) (F54*G54) /C21 H55 (F0) (F55*G55) /C22 H56 (F0) (F56*G56) /C23 H57 (F0) (F57*G57) /C24 H58 (F0) (F58*G58) /C25 H59 (F0) (F59*G59) /C26 H60 (F0) (F60*G60) /C27 H61 (F0) (F61*G61) /C28 I43 \ ----------------------- I47 \ ----------------------- I63'TOTAL INCOME:

J43 \ ------------------------------

J45"TOTAL PERSONAL INCOME J46'TO TARGET DATE J47 \ ------------------------------ J48 (B0) ((((B38/B39)*D48)-((B38/B40)*H48))/(B7-B8))*(B6-B7)+D48*D15 J49 (B0) ((((B38/B39)*D49)-((B38/B40)*H49))/(B7-B8))*(B6-B7)+D49*D16 J50 (B0) ((((B38/B39)*D50)-((B38/B40)*H50))/(B7-B8))*(B6-B7)+D50*D17 J51 (B0) ((((B38/B39)*D51)-((B38/B40)*H51))/(B7-B8))*(B6-B7)+D51*D18 J52 (B0) ((((B38/B39)*D52)-((B38/B40)*H52))/(B7-B8))*(B6-B7)+D52*D19 J53 (B0) ((((B38/B39)*D53)-((B38/B40)*H53))/(B7-B8))*(B6-B7)+D53*D20 J54 (B0) ((((B38/B39)*D54)-((B38/B40)*H54))/(B7-B8))*(B6-B7)+D54*D21 J55 (B0) ((((B38/B39)*D55)-((B38/B40)*H55))/(B7-B8))*(B6-B7)+D55*D22 J56 (B0) ((((B38/B39)*D56)-((B38/B40)*H56))/(B7-B8))*(B6-B7)+D56*D23 J57 (B0) ((((B38/B39)*D57)-((B38/B40)*H57))/(B7-B8))*(B6-B7)+D57*D24 J58 (B0) ((((B38/B39)*D58)-((B38/B40)*H58))/(B7-B8))*(B6-B7)+D58*D25 J59 (B0) ((((B38/B39)*D59)-((B38/B40)*H59))/(B7-B8))*(B6-B7)+D59*D26 J60 (B0) ((((B38/B39)*D60)-((B38/B40)*H60))/(B7-B8))*(B6-B7)+D60*D27 J61 (B0) ((((B38/B39)*D61)-((B38/B40)*H61))/(B7-B8))*(B6-B7)+D61*D28 J2"-- J63 (J0)0 @SUM(J48..J61) J64"=============

MARKETING EFFECTIVENESS OF SMALL BUSINESSES: DOES THE FAMILY MAKE A DIFFERENCE?

William J. Sauer, Bucknell University Timothy W. Sweeney, Bucknell University Philip O. Benham, Newport News Shipbuilding

ABSTRACT

This research examines the market effectiveness of small businesses. It first focuses the extent to which various marketing functions are performed and then examines the difference between family and non-family firms.

INTRODUCTION

Every year approximately 600,000 small businesses start up and, unfortunately, a similar number fail (Tate et al, 1985, p. 9). The significance of these start-ups and failures to American society should not be underestimated. Small business today is contributing significantly to the revitalization of economically depressed areas. They provide about 58 percent of the private sector jobs while possessing only one-fourth of the total business assets (Scarborough & Zimmerer, 1984 p. 3). They also provide approximately 86 percent of all new jobs (Scarborough & Zimmerer, 1984, p. 4). For every new job a community's population increases by three and one-half to four people (Sondeno, 1985, p. 12). This results in greater demand for goods and services and generates a stronger tax base and new revenues for communities. In addition, 43 percent of the country's GNP is generated by those small firms (Scarborough, 1984, p. 18). It may well be that the transformation of society from an industrial base to a technological base over the next ten to twenty years will to a large extent, be dependent on the success of small businesses. Survival for small businesses throughout the remainder of this decade and into the 1990's may well depend on the utilization of more sophisticated and formalized marketing procedures. While such factors as increasing domestic and international economic competition and the high degree of uncertainty about the future have led marketing managers of many large firms to embrace these procedures (Coe, 1981, p. 13), little, if anything, is known about the extent to which small businesses have pursued such courses of action. For the small business person the incorporation of these procedures the organizational structure may prove to be quite difficult due to lack of staff, the pressures and time required to deal with day-to-day operations and the lack of knowledge regarding these procedures (Sondeno, 1985, p. 287). In addition to these problems, the integration of formalized marketing procedures may be further impended when the business is family owned and operated. In these latter types of organizations all to often the interests of various individuals, particularly the founder or family patriarch, take precedence over the current needs of the firm (Tate et al, 1985, p. 557). Given these two sets of conditions, one would hypothesize that small business, and particularly family owned and operated businesses would not, to any great extent, utilize a wide range of formalized marketing procedures.

The purpose of this study was twofold. First, it examined the extent to which small business engaged in various marketing functions, and second, it focused on the extent to which the performance of these functions varied for family and non-family owned and operated businesses. The results of this study should provide some indication of the market effectiveness of both family and nonfamily small businesses.

METHODOLOGY

Data Collection and Sample

The data for this study were generated from a mail survey of small business firms located in central Pennsylvania. Of the 485 firms on the mailing list, 107 completed and returned the questionnaire for a response rate of 26.4 percent. These respondents represented a broad cross section of types of small business firms as illustrated by the following brief profile:

1) approximately 71 percent of the firms responding were manufacturers while 29 percent represented a mix of distributors, wholesalers, retailers, and other service-related industries;

2) seventy-five percent were private corporations, partnerships and proprietorships, and 25 percent were publicly held corporations;

3) fifty-four percent were family-owned and 46 percent non-family businesses, and;

4) thirty-five percent of the organizations employed fewer than 25 people, one-half employed between 25-100, and approximately 15 percent has over 100 employees.

Measurement

A significant portion of the research instrument and a central issue of this paper focused on marketing effectiveness. The measure of a firm's marketing effectiveness used in this research was taken from a marketing audit presented and discussed by Kotler (Kotler, 1977, p. 67-75). This approach identifies five distinct activities or components of effective marketing:

1) Customer philosophy--does management acknowledge the primacy of customer needs and wants?

2) Integrated marketing organization-is the organization staffed properly in order to carry out marketing analysis, planning, implementation and control?

3) Adequate marketing information-does management receive relevant marketing information?

4) Strategic orientation--does marketing management generate innovative plans for long- term growth and profitability?

5) Operational efficiency--are marketing plans implemented in a cost-effective manner, and are the results monitored for rapid corrective action?

The marketing effectiveness measure consists of fifteen fixed alternative questions in all, three questions per each of the five marketing components. All fifteen items represented an ordinal scale of measurement.

RESULTS

The findings of this research provide some interesting insights into the marketing effectiveness of small businesses in general, in addition to revealing both differences and similarities in the marketing orientation of non-family and family oriented firms.

Turning first to small businesses in general, Table 1, indicates that while the majority of firms (50%) recognize the importance of serving specific market segments, only about one-third strongly emphasize developing different offerings and plans for each segment and/or taking systems of view of marketing which focuses on threats and opportunities which permeate the entire market channel. With regards to integration, it can be observed that while marketing is well integrated with other functional areas in most firms (57%), the major marketing functions themselves appear to be highly integrated in only 36% of the firms, with only 24% stating that a well organized new product development process was in place. The gathering and use of marketing information, however, tends to be one of the strong features of small businesses. Approximately 60 percent of the firms in the study indicated that they had recently conducted studies focusing on customers, buying influences, channels and competitors. In addition, 50 percent felt they had a very good understanding of sales potential and profitability with regards to different markets. Less than one-third, however, indicated any substantial effort being expended to determine the cost effectiveness of different marketing expenditures. Perhaps the area in which small businesses demonstrated the greatest weakness was that of strategic planning. Only one- quarter to one-third of the firms in the study indicated a strong propensity towards high quality formal planning that incorporated contingency plans should they be necessary. Finally, with regard to the operational efficiency, most firms fail to communicate very effectively their marketing thinking from the top down, to use their marketing resources effectively, or react effectively to rapid changes.

In summary, while overall, small firms tend to show some strengths with regard to their customer philosophy and the gathering of significant information they tend to manifest a fairly high degree of inadequacy with regard to those dimensions of market effectiveness, such as integration, strategic planning and operational efficiency on which their survival may ultimately depend.

The findings of this research further revealed both differences and similarities in the marketing orientation of family and non-family small businesses.

Turning first to the differences, (Table 1) several interesting findings emerged. Non-family businesses were significantly more likely to recognize that different market segments existed and as a result realized the importance of organizing the company to meet the needs of those segments of interest to them. As a result of this recognition, non-family businesses were also more likely to develop different offerings and different plans for those segments with which they intended to interact. Given these findings, it was not surprising that the non-family business tended to feel that they were better organized with regard to new product development and more likely to indicate that they did more market planning and more detailed planning than did family-owned businesses.

While the differences between family and non-family businesses focused more on consumer needs and planning to meet those needs, the similarities focus more on general marketing strategy. The findings with regard to similarities fall into two categories; those which both seem to be doing to a fair degree, and those which both seem to be overlooking.

In the case of both family and non-family operated businesses there appears to be a significant amount of concern with the integration of various marketing functions. Both groups felt that the various functional groups in the company worked well together, that they had the necessary research to understand various markets and their potential and that they understood the nature of the markets, their needs, and the distribution systems required to meet those needs.

In addition to those tasks which both family and non-family businesses appear to engage with some degree of regularity, there are also several functions which appear to get very little attention. The data reveal that neither group adheres to a holistic marketing system view. Consequently, it was not surprising to find that to a large extent they tend not to engage in such activities as examining the cost effectiveness of different marketing expenditures, innovative data based strategy planning, contingency planning, implementation of strategies, management of marketing resources or reacting to unexpected developments.

In summary the data suggest that non-family operated small business are more likely to be perceptive of consumers needs, choose target markets and develop plans to meet those needs. At the same time both groups appear to engage quite actively in those tasks required to bring the product to the marketplace, but neglect those aspects of the larger marketing system.

IMPLICATIONS

The results of this research have marketing implications for small business firms in general as well as for family-owned businesses specifically. Generally speaking, small business firms must extend themselves beyond attitudinal and informational commitments to the marketing function and begin to plan, implement and operationalize marketing programs targeted towards specific market segments. The data seems to suggest that small business organizations understand the importance of the marketing function, but have yet to commit the time, energy and resources necessary to have established marketing as the driving force in their businesses.

With respect to family versus non-family businesses, it seems that family-owned organizations need to examine their basic approach to marketing decision-making. It is clear that non-family firms employ marketing strategy planning to business decision making; this is, identifying specific segments of opportunity and developing marketing mix programs to appeal to these targeted segments. Family-owned businesses, however, are less likely to design and implement marketing strategy plans. While there are insufficient data in this study to explain the reasons for these differences, one might speculate that the culture of family businesses characterized by potentially complex family relationships inhibits formal business planning practices. Whatever the plausible explanation, there is ample evidence in these findings to suggest the need for all individual small business firms to conduct an audit of marketing effectiveness as a way of identifying some strengths and weaknesses of the marketing function within their respective organizations.

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TABLE 1 MARKETING EFFECTIVENESS BY NON-FAMILY VS. FAMILY OWNED BUSINESSES

NON- Customer philosophy TOTAL FAMILY FAMILY SAMPLE OWNED OWNED A. Does management recognize the im-- (N=107) (N=49) (N=58) portance of designing the company to serve the needs and wants of chosen markets? Score Management primarily thinks in terms 0 23.4 14.3 31.0 X(2)=7.35 of selling current and new products S=.02* to whoever will buy them.

Management thinks in terms of serving 1 27.1 22.4 31.0 a wide range of markets and needs with equal effectiveness.

Management thinks in terms of serving 2 49.5 63.3 37.9 the needs and wants of well-defined markets chosen for their long-run growth and profit potential for the company.

B. Does management develop different offerings and marketing plans for different segments of the market?

No. 0 11.2 6.1 15.5 X(2)=4.68 S=.09 Somewhat. 1 58.9 55.1 62.1

To a good extent. 2 29.9 38.1 22.4

C. Does management take a whole marketing system view (suppliers, channels, competitors, customers, environment) in planning its business?

No. Management concentrates on 0 14.0 10.2 17.2 X(2)=1.66 selling and servicing its immediate S=.43 customers.

Somewhat. Management takes a long 1 54.2 53.1 55.2 view of its channels although the bulk of its effort goes to selling and servicing the immediate customers.

Yes. Management takes a whole 2 31.8 36.7 27.6 marketing systems view recognizing the threats and opportunities created for the company by changes in any part of the system.

Integrated marketing organization

D. Is there high-level marketing in- tegration and control of the major marketing functions?

No. Sales and other marketing func- 0 16.8 12.2 20.7 X(2)=2.09 tions are not integrated at the S=.33 top and there is some unproductive conflict.

Somewhat. There is formal integra- 1 46.7 44.9 48.3 tion and control of the major market- ing functions but less than satisfac- tory coordination and cooperation.

Yes. The major marketing functions 2 36.4 42.9 31.0 are effectively integrated.

E. Does marketing management work well with management in research, manufacturing, purchasing, physical distribution, and finance?

No. There are complaints that market- 0 8.5 6.7 10.2 X(2)=0.75 ing is unreasonable in the demands S=.68 and costs it places on other depart- ments.

Somewhat. The relations are amicable 1 34.0 37.8 30.6 although each department pretty much acts to serve its own power interests.

Yes. The departments cooperate 2 57.4 55.6 59.2 effectively and resolve issues in the best interest of the company as a whole.

F. How well-organized is the new product development process?

The system is ill-defined and poorly 0 27.4 15.6 38.0 X(2)=6.03 handled. S=.04*

The system formally exists but lacks 1 48.4 55.6 42.0 sophistication.

The system is well-structured and 2 24.2 28.9 20.0 professionally staffed.

Adequate marketing information

G. When were the latest marketing re- search studies of customers, buying influence, channels, and competitors conducted?

Several years ago. 0 23.5 17.0 29.4 X(2)=2.63 S=.26 A few years ago. 1 18.4 17.0 19.6

Recently. 2 58.2 66.0 51.0

H. How well does management know the sales potential and profitability of different market segments, custom- ers, territories, products, channels, and order sizes?

Not at all. 0 6.7 4.2 8.8 X(2)=2.43 S=.29 Somewhat. 1 44.8 39.6 49.1

Very well. 2 48.6 56.3 42.1

I. What effort is expended to measure the cost-effectiveness of different marketing expenditures?

Little or no effort 0 24.5 22.9 25.9 X(2)=0.26 S=.87 Some effort 1 45.3 47.9 43.1

Substantial effort. 2 30.2 29.2 31.0

Strategic orientation J. What is the extent of formal marketing planning?

Management does little or no formal 0 41.5 31.3 50.0 X(2)=7.29 marketing planning. S=.02*

Management develops an annual 1 33.0 31.3 34.5 marketing plan.

Management develops a detailed annual 2 25.5 37.5 15.5 marketing plan and a careful long-range plan this is updated annually.

K. What is the quality of the current marketing strategy?

The current strategy is not clear 0 30.2 25.0 34.5 X(2)=1.14 S=.56 The current strategy is clear 1 50.9 54.2 48.3 and represents a continuation of traditional strategy.

The current strategy is clear, 2 18.9 20.8 17.2 innovative, data-based, and well- reasoned.

L. What is the extent of contin- gency thinking and planning?

Management does little or no 0 7.5 6.1 8.6 X(2)=204 contingency thinking. S=.35

Management does some contingency 1 64.5 59.2 69.0 thinking although little formal contingency planning.

Management formally identifies 2 28.0 34.7 22.4 the most important contingencies and develops contingency plans.

Operational efficiency

M. How well is the marketing thinking at the top communicated and implemented down the line?

Poorly. 0 12.6 10.4 14.5 X(2)=1.01 S=.60 Fairly. 1 50.5 47.9 52.7

Successfully. 2 36.9 41.7 32.7

N. Is management doing an effective job with the marketing resources?

No. The marketing resources are 0 19.8 12.5 25.9 X(2)=4.15 inadequate for the job to be done. S=.12

Somewhat. The marketing resources 1 54.7 64.6 46.6 are adequate but they are not employed optimally.

Yes. The marketing resources 2 25.5 22.9 27.6 are adequate and are deployed efficiently.

O. Does management show a good capacity to react quickly and effectively to on-the-spot developments?

N. Sales and market information 0 6.5 4.1 8.6 X(2)=1.65 is not very current and management S=.44 reaction time is slow.

Somewhat. Management receives fairly 1 59.8 57.1 62.1 up-to-date sales and market information; management reaction time varies.

Yes. Management has installed systems 2 33.6 38.8 29.3 yielding highly current information and fast reaction time.

* indicates significance at the .05 level.

MARKETING THE SBI PROGRAM: A UNIQUE APPROACH USING AN SBI TEAM A WORKSHOP

Alice N. Griswold, University of Dubuque

ABSTRACT

This paper presents how a small school used an SBI student team to develop a promotional campaign for its SBI program. Included is a discussion of the methodology used, pros and cons of using a student team, and guidelines regarding media selection and message. Actual examples of material developed are included with the hope that other SBI directors will find this inform-

ation useful when embarking on a promotional campaign of their own.

INTRODUCTION

Promoting a university's SBI Program in order to obtain good clients and develop a positive image in the business community has been a problem long plaguing directors of smaller, less urban schools. This is primarily due to the small industrial base and fewer SBA borrowers in these areas. A large university SBI director may face difficulty in obtaining clients for a different reason - lack of time. Typically, the SBI director is a faculty member carrying a full teaching load and is expected to do research and publish as well. For all these reasons, it becomes necessary to "market" the SBI program to the community. The benefits of doing such are numerous:

-Small businesses become aware of a consulting service available to them through the SBA at no charge. In rural communities heavily dependent on the agricultural market, such as ours, many small businesses are struggling and cannot afford to pay the several thousand dollars a company would charge for market research, or an ad campaign. The SBI consulting service not only increases the businesses' likelihood of succeeding, but also boosts the image of the SBA (an area of major concern lately) and the University offering the SBI program.

-The SBI program can serve as a link between the business department of the University and the business community. Too often, these two groups have virtually no contact with one another which furthers the notion that theoretical classroom learning and the 'real world' have little to offer one another. A strong relationship between the SBI program and the business community serves to bridge the gap between these two camps. Clients serve as teachers of real world business problems, and receive the benefits of the students' theoretical learning in accounting, marketing, finance, and management. The SBI program, in return, receives recognition in the business community as a result of their outreach program and has a source of small business owners and managers who might serve as resource persons to students as well as speakers in the classroom.

-Personnel managers in the community become aware of a college program giving students the opportunity to do consulting for a business. This practical experience may be what gives a graduate from an SBI program an edge in the job market.

Few SBI directors would argue with these benefits resulting from promotion, however most would find it difficult to devote the necessary time and creative energy it takes to successfully launch such a marketing effort.

The idea to embark on a formal marketing campaign for our SBI program using SBI students was not born overnight. In 1983, we used an SBI team to investigate various promotional tools that could be used for the SBI program at the University of Dubuque. The results of their field work determined that public service announcements and features were best for us, as they were free, easy to implement, and would cover a wide market area. In spite of the excellent work and detailed promotion plan of the SBI team, the directors were unable to implement the plan at the time because of teaching commitments which took precedence. However, in January 1986, the proposed plan came off the shelf as the directors felt the university's SBI program needed greater publicity. As a secondary benefit, it was hoped that the campaign would assist in developing a more positive image of the SBA in the community. It also had come to our attention that some of our own University faculty felt we weren't getting enough visibility regarding this excellent program. Thus, we decided to designate an SBI team in January 1986, with the sole purpose of developing and implementing a promotion campaign for our SBI program.

DEVELOPING THE CAMPAIGN

An SBI team of three undergraduate students and a graduate student advisor were assigned the semester project of marketing the Small Business Institute. They were given a copy of the 1983 SBI team's recommendations as a starting point, and a budget of $150.00. Although the students were already familiar with the SBI program, time was taken to discuss the role of SBI at the university, in the community, and on a national scale. The team was further advised that they were to generate a list of available media channels, make the necessary contacts with the media and set up a schedule of media events that were to occur during the semester, as well as a timetable for future promotional releases. They were advised that the SBI director and the University Public Relations Office were available to assist and advise them and that all final copy needed approval by these two sources before being released to the media.

FEATURES OF THE CAMPAIGN

Press Release

The press release was the first promotional tool developed. it was a one page fact sheet that was to be sent to all area advertising media which offered public service announcements. It answered basic questions about the SBI program such as:

- What the program does? - Who sponsors it? - What it costs? - Who does the consulting? - Who is eligible to receive a team? - What areas can be addressed? - When the services are offered? - Who to contact?

The release was mailed to approximately 20 area newspapers and radio stations, area television stations (Group W Cable and KDUB Channel 40) for public service announcements, and three of the local retail trade associations for use in their newsletters. In addition to this, the Dubuque Chamber of Commerce was given a copy so they could run a feature on the SBI program in their monthly newsletter, PROFILE, whenever space is available. A copy of the press release can be found in Appendix I.

NEWSPAPER

Since the Dubuque area is served by only one major paper, The Telegraph Herald, the choice of newspaper was simple. However, there are several different types of promotion available through this medium.

1) Civic Page

This page runs once a week and is utilized by non-profit organizations at no charge to them. The ad is over half a page in size and is therefore popular among these organizations. Arrangements for this ad need to be made approximately six months in advance. Our ad appeared December 1, 1986, which was timed to generate clients for our Spring 1987 semester. The newspaper staff prepared an artist's layout of the ad a few weeks before publication which was proofed by the SBI directors. This copy can be used for future civic pages as well. The advertising space value of the Civic Page is approximately $400.00.

2) Paid Advertising

Although funding was limited, the students chose to run an ad in the business section of the paper during July. A combination of a Tuesday and a Sunday were chosen to attain maximum exposure (weekday and Sunday paper). The University has a retail advertising contract with the news-

paper, which allows for discounted rates. The SBI ad went through this account resulting in a total cost of $84.00 for a 3" x 3" ad for two days.

The students designed the ad using the university logo in one corner and "Consulting for Small Businesses" as a heading. There was considerable discussion whether the words 'free service' should be included, as there was concern that it might "cheapen" the SBI image. As a result, the phrase "at no charge" was included in small print to avoid losing businesses who were experiencing financial difficulties. After this debate, the newspaper ran the ad omitting "at no charge" in error! They agreed to run the corrected ad at no additional cost. Copies of the ads can be found in Appendix

II.

3) Feature Article

The newspaper was approached to see if they would be willing to do a feature article explaining the SBI program in greater detail. The contact person at the paper was the local news editor, who in turn assigned the story to the business writer. She felt it was a good topic - both newsworthy and a service to local businesses. September 1986 was the first opening in the schedule. The SBI directors, selected former and current SBI students, and several previous clients were assembled for the interview, which took about one hour. The reporter was also given names of several other previous clients and students to contact for further information. To maintain confidentiality of the clients, the SBI directors contacted previous clients before the interview requesting permission to release their names to the reporter. Any additional client information would come only from an interview between the client and the reporter. The SBI directors further requested to proof the article before publication to be certain of no breach of confidentiality. The article appeared on September 15, 1986. A copy of the article can be found in Appendix III.

RADIO

By contacting local radio stations, two interviews were scheduled during May 1986, on the SBI Program. These stations were chosen due to their high listenership amongst local merchants and businesses.

1) WDBQ - "Pulse of Dubuque"

This program is a half-an-hour interview show that is run Monday through Friday at 12:30 and again at 5:30 p.m. It focuses on community concerns and is for use by non-profit organizations. During this interview, SBI directors and students were present and telephone lines were open for questions.

2) KDTH - "Today In The Tri States"

This program is a 20 minute interview which also focuses on community affairs. It is broadcast at 9:10 a.m. The format was identical to the first interview. In both cases, a fact sheet concerning the SBI program was delivered to the radio stations preceding the interviews. A partial transcript of the broadcast can be found in Appendix IV.

BROCHURE

A new brochure was designed utilizing the SBA's current brochure as a guide. The main objective was to personalize the brochure for the University of Dubuque. It would be used by the directors of the program to provide prospective SBI users with basic information. Ten brochures were sent to the Dubuque Chamber of Commerce (as well as 20 other Chamber of Commerces in surrounding towns) with a letter explaining the program and asking them to make the brochures available to businesses that might be interested. Area Retail Trade Associations were also sent ten brochures for distribution. The printing cost (through the University of Dubuque printing office) was approximately $4.00/100 brochures. Paper weight (for mailing purposes) as well as color decisions were carefully deliberated by the SBI team. A copy of the brochure can be found in Appendix V.

T. V.

Because of the cost of T.V. advertising, this form of promotion was not an option. The possibility of doing a feature film was explored and may be pursued at a later date, but at this time limited interest was expressed. T.V. station KDUB did receive a copy of the press release and has been requested to use this for public service announcements.

CONCLUSION

The purpose of this paper was to share with other SBI directors a method by which SBI programs could be promoted using a low budget and minimizing a faculty member's time. The unique approach involving the use of SBI student teams to develop a promotional campaign has several advantages:

-Students get an opportunity to market a product they are involved in and familiar with.

-Media analysis, selection and timetables are done by the students. They make the necessary contact with the media spokespersons and actually develop the message (print copy).

-The complete written report is a carefully analyzed and formally organized promotional campaign that allows an on-going marketing effort by SBI directors.

-Students get personal exposure and experience with the media which is valuable to them in their own job search.

A review of all the materials developed and implemented indicates that the SBI team was very successful in meeting the objectives for their case. Feedback from the business community, university faculty and staff, and previous clients has been very positive. The promotion has created awareness of the SBI program in the community and yielded numerous inquiries over the past few months. Some of these inquiries are from businesses who are not bordering on bankruptcy or making a last ditch effort to save themselves, but rather are in strong financial shape. They are eager to strengthen their position and want our assistance in computerizing their records or developing a new ad campaign. Our client roster is increasing and we feel our relationship with local business organizations has improved greatly. Comments by representatives of the media and the University's Public Relations Director indicate that they feel the students produced a promotional campaign of professional quality. Furthermore, the SBI team pursued all possible media channels in spite of difficulties reaching the necessary contacts, tight schedules, and unforeseen delays and errors all of which are everyday occurrences in the advertising world. An evaluation by the SBI students themselves generated positive comments about the real world experience, the ability to actually see their promotion ideas in use, and the valuable knowledge gained through writing press releases, designing ads and brochures, and being interviewed on live radio. Negative comments included time limitations and the long hours spent pursuing all media alternatives. At this point, all the promotion material will be turned over to the University's PR office for future implementation. The total cost for the campaign was:

Civic Page 0 Radio Interviews (2) 0 Feature Article 0 Brochure printing 4.00 Press release mailing 20.00 Newspaper Ad 84.00 TOTAL $ 108.00

A figure well under the budgeted $150.00

Obviously a promotional campaign such as this should not be the sole means of advertising. The SBI program does require some personal contact on the part of the SBI director with the business community, service clubs and retail associations. However, promoting the SBI program using an SBI team has proven to be, for us, a very time and cost effective way to reach our market. It is hoped that the information in this paper will assist other SBI directors in conducting their own campaign.

APPENDIX I

UNIVERSITY OF DUBUQUE 2000 University Avenue, Dubuque, Iowa 52001 319-589-3000

FOR IMMEDIATE RELEASE May 5, 1986

Contact: Alice Griswold Assistant Professor, Administration and Business University of Dubuque 2000 University Ave. Dubuque, IA 52001 (319)589-3193

Dubuque, Iowa - The Small Business Institute of the University of Dubuque offers consulting services to businesses in the Dubuque area.

The Small Business Institute is a management assistance counseling service offered by the Department of Business Administration at the University of Dubuque through the U.S. Small Business Administration. Services are provided without charge to participating businesses.

Qualified, upper-level business students are organized into small teams, under faculty supervision. They meet with the business owners/managers to study the strengths and weaknesses of the business to determine an appropriate course of action. All services are confidential.

Consultation has been given in the following areas: * Accounting and Finance * Buying and inventory control * Selling and advertising * Management and business strategy * Personnel administration * Location selection * Product development * New business analysis * Computerization

The University of Dubuque is currently accepting businesses for the fall semester of 1986.

For more information, or to set up an appointment to find out how to put a Small Business Institute team to work for your business, please call or write: Alice Griswold or Candace Humphrey University of Dubuque 2000 University Ave. Dubuque, IA 52001 (319)589-3193

APPENDIX II

Newspaper Ad Appeared July 22 and July 27, 1986

CONSULTATION FOR SMALL BUSINESSES now available through the Small Business Institute of the University of Dubuque.

For more information, or to put an SBI team to work for your business, Call: Alice Griswold Asst. Professor Business (319) 589-3193 1000 University Ave., Dubuque The Small Business Institute is a program of the US. Small Business Administration

Original Ad

CONSULTING FOR SMALL BUSINESSES at no charge now available through the Small Business Institute of the University of Dubuque. For more information, or to put an SBI team to work for your business, Call: Alice Griswold Asst. Professor Business (319) 589-3193 1000 University Ave., Dubuque The Small Business Institute is a program of the U.S. Small Business Administration

Corrected version - included "at no charge" Total cost - $83.99

APPENDIX III

By Sue Blocker of the Telegraph Herald

After eight years, the Small Business Institute is taking its own advice to market its services.

The University of Dubuque sponsored program opened in 1978 to offer consulting services to area small businesses. The free counseling program is affiliated with the Small Business Administration.

"We got the feeling that we're not real well known," said Alice Griswold, one of the program's directors. "That's when we decided to advertise."

The Institute began a campaign this spring. Business people's responses verified Griswold's suspicions. "Most were saying, 'I never even knew this existed.'"

The Institute offers guidance for businesses that might not have anywhere else to go, and, at the same time provides students with valuable training, said Griswold and co-director Candace Humphrey.

Based on grade point averages and faculty recommendations, the Institute invites 15 to 18 seniors and graduate business students to handle the 4 to 6 cases each semester.

Griswold and Humphrey match students to cases depending on the area of expertise needed.

"Teams" of students then help businesses with services - setting up accounting system, marketing plans, promotions, computer systems.

After meeting with the students and clients, the directors let the students take over. But advice availability continues throughout the semester, Humphrey said.

Jane Miller is in her second semester at the Institute.

She wasn't intimidated by the idea of trying to help professional business people. She was enthusiastic.

"You can sit in a classroom all you want, but it's that real experience every student should have," Miller said.

Marilyn Kammiller agreed.

Listing experience with the Institute on her resume helped Kammiller land a job at Frommelt Industries in Dubuque.

She helped Stella Haun at the Butcher Shop in Dubuque when Haun and her husband opened the business in 1983. Kammiller set up a double-entry bookkeeping system for the Hauns. The next semester she helped them prepare tax returns.

Kammiller went back on her own a third time to help again with the books and prepared a booklet Haun could follow to do the job on her own.

Writing the booklet "made me feel so proud. It gave me a feeling of accomplishment," Kammiller said.

Griswold added, "Students find out very quickly they know a lot more than they thought."

Although it helps students, the Institute's emphasis in on businesses, she said. "We are not doing this first and foremost for the students."

The first rule is: Businesses are assured of confidentiality. The Institute will not disclose names of its clients without permission.

Another requirement is that students prepare a detailed report of their findings and recommendations at the end of the semester.

When the Esther Hillman House apartment complex opened in East Dubuque two years ago, students did a marketing study on elderly housing, said Hillman's project manager Lisa Barklow.

The final report helped Hillman House devise a marketing strategy, Barklow said. "They went over it from cover to cover. We will always have that to go back on," she said.

The Institute has also counseled established businesses like the 60-year old Brannon Monument Co. in Dubuque. Mary Lou and Vincent Brannon had operated the business 25 years, but wanted to be sure their methods were best for their customers.

"It gave us some confidence knowing our advertising was adequate and our location was adequate," Mary Lou Brannon said.

After 25 years of business, it helped to meet and hear suggestions from people with a fresh perspective, Brannon said.

Cases aren't as pleasant when teams must recommend a client go out of business, Griswold said.

But whether its helping on business get started or another close its doors, the Institute offers services many clients might not have afforded otherwise.

"Small businesses don't have that many places to turn," Griswold said.

APPENDIX IV

Radio Interview Partial Transcript

Announcer: What is the program all about?

Answer: The program has been going since 1979. We have had clients every semester since that time. We have been active in the program and we will continue to be active in the program.

Announcer: Why did this all come about?

Answer: We felt that the University of Dubuque could offer a service to businesses in the Dubuque area. This is a program through the Small Business Administration that is run through the universities. It allows students in their Junior or Senior year to act as consultants to the businesses in the area and assist them in the management of their business. We felt that this is a valuable service to small businesses in this area.

Announcer: Can we say there are other colleges in Iowa that are participating in this?

Answer: Yes.

Announcer: Across the nation, is there a whole network?

Answer: Yes, the Small Business Institute is a national program offered through the Small Business Administration through universities. In Eastern Iowa alone, we have seven universities that offer this program.

Announcer: As a network do you trade information, experiences, or results? Maybe have a convention once a year where the directors and students get together and share what they have learned?

Answer: Yes, Small Business Institute Directors Association had a convention in February in Washington D.C. This gives the directors in the universities a chance to get together and talk about the program, how to serve different businesses better, and making the experiences for the students better.

Announcer: From all the stuff that I have read, they say that more and more young people are going into business majors in colleges. So it would appear that you probably don't have a lack of people for these programs?

Answer: No, we do not, however, we do limit the program to our top students. It is by selection in our program only. In other words, we take a look at their grade point average, in terms of their leadership ability, and the ability to conduct themselves in a professional manner. So it is a program that we do by invitation only.

Announcer: How are the businesses in Dubuque and the surrounding areas? Have they been real receptive to the program?

Answer: We feel they have. We realize that a lot of small businesses are not aware of this program. This is partially the reason we would like to get this information out. The businesses that have used our service have been in general very pleased with it and have been, I think, impressed with the student participation and quality. I think this is positive sign.

Announcer: Are there any limitations of what kind of businesses you will work with, say size of the business, what the business is in and what the business is doing?

Answer: Yes, there are some limitations. Generally it is difficult to define all in one grouping. However, in the Dubuque area most businesses will qualify. For retail concerns, we are looking at businesses that have total annual gross sales less than $2 million or employees somewhere in the range of less then 250 so that would mean that most businesses in this area would qualify.

Announcer: Regarding-businesses that have participated in the program, did they come to you and say, hey, I feel I have a problem with this aspect of my business and wonder if your group of people can help me deal with it? Do they approach you that way?

Answer: They come to us in a variety of ways. Some of the clients that we get are referred to us through the SBA regional office in Cedar Rapids. Some have contacted us simply from hearing about us, saying we have a problem could you help us with it. Some have talked to other small businesses who have used our services. So it is both through referrals of other businesses or through the SBA office in Cedar Rapids.

Announcer: All the information is kept confidential?

Answer: Absolutely.

Announcer: What have been some of the problems that they have had you work on?

Answer: I would say the majority of our services would be in the marketing area. We conduct marketing surveys, market research, promotional campaigns. We have done product analysis. We have looked at inventory. We have looked at personnel problems and location decisions. One of the newer areas that we have been looking at has been the area of computers. The utilization of computers for business.

Announcer: So right now how many students are participating in the program?

Answer: This semester we have eight students and six cases.

Announcer: Are they working as teams or individuals?

Answer: Teams, we try to keep it to teams of two or three. That way they can meet more often and really work as a group. . . .

TRAINING FOR SALES IN THE SMALLER BUSINESS A NEED FOR RE-EXAMINATION?

Stephen J Pettitt, National Institute of Higher Education, Limerick, Ireland W Gerald Kirkwood, Teesside Polytechnic, UK

ABSTRACT

This paper reviews how personal selling helps the small firms marketing effort. It follows an electic approach and argues that sales training by concentrating on the operational level can directly encourage greater receptivity to broad based marketing and implementation. Whereas marketing trainers tend to emphasize strategic concepts and frameworks that are difficult to apply in a less sophisticated environment the approach outlined, by starting where the trainee is at with scarce resources to meet operational pressures, may encourage both improved operational marketing effectiveness and progress towards revised strategic marketing thinking.

INTRODUCTION

The small business support infrastructure in both the UK and Ireland usually incorporates an element of training in management skills and techniques. Although topics may vary to suit local needs and resources, often they would include financial control, legal issues, employing staff and venture appraisal. Marketing may be introduced as part of a comprehensive training program or as a specialized course in its own right. In the UK a range of programs sponsored by the Manpower Services Commission (MSC), Local Authority or the private sector operate at start- up, expansion and regeneration stages in small firm development. Similarly in Ireland, although with a somewhat greater bias towards manufacturing and internationally traded activities, a comprehensive training framework has developed. Many colleges, polytechnics and some universities act as key providers and this commitment is likely to strengthen as small business, with its perceived employment potential, continues to attract national and international political interest.

Although a large number of institutions do have some involvement with the smaller firm (1) it has been argued by some writers that there needs to be more relevant specialization in structures, processes and content if the real needs of the small business training market are to be met (2). However few would disagree with the importance and critical role that marketing training and education should have within overall learning frameworks.

From the standpoint of small firms themselves the relative emphasis on particular marketing postures often varies for the individual business according to a wide range of internal and external influences. These would typically include product forms, technological processes, organizational size and structure, growth rates, personal/management styles and activities, markets served, trading practices and levels of competition. Such diversity is unlikely to be specifically addressed at an individual level in the design of general training programs for small businesses. Instead, the diversity may be merely reflected in the provision of broad conceptual frameworks including the strategy of products, markets, positioning etc and operational implementation of pricing, promotion, distribution and the need to sell into specified markets. It is this need to sell and the role of selling within new and developing small businesses that often poses a major challenge arising from their dependence on external customers' acceptance of a proposed product or service.

Such a challenge often creates both external and internal tensions as plans fail to materialize into reality. Even within larger organizations the relationship between marketeers and salespeople has been problematic. The logic as proposed by MacDonald (3), of course, is indisputable: "unless a good deal of careful marketing planning has taken place before the salesman makes his effort to persuade the customer to place an order, the probability of a successful sale is much reduced". But despite the logic, there often appears a gulf in background, culture and perspective between sales and marketing personnel. Marketeers are often accused of being 'out of touch' with customers, excessively analytical and disparaging about the relative contribution of the sales team. Meanwhile sales personnel are criticized by marketeers for short term thinking, a lack of direction and planning and sometimes downright unprofessional selling activity. No such organizational conflict is likely to exist within the average small firm, especially where no full time specialist sales and marketing personnel are employed. However the potential does exist for the above distinctions to be internalized by the owner-manager performing a multi-functional role. Sales are immediate, marketing can often be left for tomorrow, even though it is recognized that a variety of promotional methods can be adopted to attract new business.

Although this paper accepts a balanced view of the need for both selling and marketing thinking within small firm development it maintains that in many development systems the former is conspicuous by its absence. Perhaps it is almost paradoxical that although the need to sell effectively has been recognized by both small business practitioners and advisors alike, many of the skills and techniques of professional selling are given only cursory treatment in start-up and expansion programs. Wide experience with small firms in both the North East of England and Ireland suggests to the authors that many new starters, and a number of existing businesses lack many of the basic skills in implementing their marketing plan through effective salesmanship.

Just how valid is it to give low priority to effective salesmanship in small business training programs? The need for raised levels of marketing thinking within small firms is widely recognized in both Europe and the USA, but what about the need for better selling skills? Can the assumption be made that skills in listening, questioning, presenting, persuading, handling objections and closing sales are already well developed from previous commercial or life experience? It could be argued that although selling is the climax of a wide range of marketing activity and can be made easier or more difficult by previous mix / strategic decisions, the reverse may also hold true. However effective the formative decisions, a failure to contact / research key buyers, to make persuasive presentations and to close the sale, will mean that the overall objective cannot be realized. There is nothing like a potential customer saying "No" to focus the mind of a new starter on the need to transfer concepts and plans into reality!

LITERATURE REVIEW

In this paper sales training for the owner-manager is taken as a specific intervention designed to raise effectiveness within businesses which are too small to employ full time sales specialists. As such no body of literature exists examining this applied area of study in terms of role, contribution, structure, processes and overall effectiveness in assisting small firm selling and thus business development activity. However the conceptual and empirical work undertaken in a number of related and perhaps contributory areas of study are worthy of attention in developing a sales training 'model'. Four areas have been selected to examine the conceptual basis for a sales training model: marketing, personal selling, small business management and management development. Each contribution is likely to differ regarding the content and process of sales training programs within the applied area of non specialist, small business training. These relationships are outlined diagrammatically in Exhibit 1.

Small Business Management Marketing

Sales Training for the Owner-Manager

Management Development Personal Selling

Exhibit 1: The Conceptual Bases for a Sales Training Model

(a) Marketing

Despite the recognized criticality of marketing in small firm development it is perhaps surprising how little attention has been paid to constructing a conceptual framework that integrates and focuses the main body of marketing literature towards the smaller firm. Although it is unlikely that any new principles of marketing will emerge, the need for an 'applications engineering' approach, reflecting such issues as multi-functional roles, lack of resources and specialist personnel, limited control of environment, informal control systems and limited market impact, needs to be developed.

A number of recent studies in Ireland and the UK have highlighted some of the dimensions of poor marketing performance. In Ireland a major study was recently completed into 'Ireland and Marketing' (4). The findings were generally depressing. Weaknesses were identified, particularly with small manufacturing firms, at both a strategic and operational level. Although there are inherent methodological dangers in generalization about the small firms sector, the report found problems in the following areas:

* Poor competitive positioning * Limited product innovation * Over dependency on selected customer / markets * Over emphasis on price as a competitive weapon * Poor selection of distribution channels * Wasteful and uncreative promotional activity * Low levels of personal selling skills.

These findings were broadly in line with earlier research by Ford and Rowley (5) in the UK and the European Management Forum Report (6). In the UK and Ireland a consensus is emerging in support of the general shape / dimensions of the problem but as pointed out by Pettitt and Kirkwood (7) in a review of marketing support interventions, somewhat less agreement and indeed understanding exists as to the most appropriate form and intensity of assistance.

Researchers in the mainstream of marketing theory and management practice either fail to recognize the contexturial differences of scale of operation or prefer to concentrate on discipline based issues. Such work (segmentation models, consumer behavior, advertising processes etc) is essential to the emergence of a more rigorous discipline particularly when marketing itself, as a business discipline, is still a relative newcomer. However what has been generally lacking, yet needed to support the growing interest in the small firm sector, is an 'applications engineering' approach linking theory development to sound management decision making within the small firm. It could be concluded that the contribution of marketing research to small business management, let alone specific sales training remains in its infancy.

(b) Personal Selling

Empirical research into the personal selling and sales management activities of the owner manager generally has been sparse. Even in the main body of literature of selling some concern about the quality of material has been suggested. Grikscheit et al (8) commented that "despite its patent importance, the professional literature on selling is one of the 'dark corners' in marketing. More often than not books and articles about selling either attempt to capture the successful experiences of the star salesmen or contain exhortations which, allegedly, will aid the salesman's rise from mediocrity to greatness".

Of course extensive literature does exist on the training and development of professional salesmen (9; 10; 11; 12; 13; 14), but again there is little empirical evidence to support many of the methods proposed beyond the particular situation for which they were developed. Dubinsky (15) expressed concern over the lack of a 'theory' of sales training and called for a 'great deal of additional empirical research and theory building' to enable better designed / implemented activities. Against such a backcloth of mystique, folklore, specialized in-company approaches and only a slow emergence of a more rigorous approach, it is perhaps not surprising that small business trainers remain to be convinced of an appropriate role and approach for incorporation of selling within their programs.

(c) Small Business Management

Even a brief review of some of the standard texts on Small Business Management reveal a perspective that is both shallow and narrow. A number of examples may illustrate the point. Olm and Eddy (16) in a comprehensive review of the stages in venture management make only an oblique reference to the need to implement an effective selling approach by suggesting that failure may derive from the entrepreneur 'not having the ability, the means or the persistence to market the product successfully' (pg 198).

Schollhammer and Kurcloff (17) identified that personal selling, "a conversation with one or more prospective customers for the purpose of making a sale, plays a key role in the marketing effort of most small businessmen". Despite such a key role, little elaboration of small business owners in a direct selling role is contemplated. Siropolis (1-8) concluded that "advertising rarely closes the sale. So entrepreneurs must also rely on personal selling. That means meeting customers face to face to help make up their minds". Again the elaboration of this process is skeletal, the perspective adopted being from a sales management orientation (recruitment, compensation, control etc). Such a perspective is based on the assumption that small firms will employ salespeople. In the UK, and particularly in Ireland, with different concepts of smallness then in the US, it is more likely that the owner manager himself will be actively involved in direct selling.

A more recent text by Ames and Wellsfry (1-9) devotes a whole chapter to 'Selling Your Product or Service' and does take a more pragmatic view of the selling process within the smaller firm. Although the empirical base of this work appeared limited and perhaps overdue emphasis was given to managing the selling effort through employed sales people, some consideration was given to selling techniques and tactics.

Vesper (20) adapts a realistic perspective by highlighting the need to obtain orders and 'not to just assume it away' in the start-up process. However the recommendation to refer to texts on salesmanship and marketing (pg 110) fails to suggest a credible option for the small business reader. It is interesting to note that the tendency to suggest 'read elsewhere' often characterizes the low level of selling insights, yet considerable detail is entertained in such areas as premises, bookkeeping, computers etc. Why this should be is an intriguing question requiring future careful enquiry.

(d) Management Development

A large volume of research evidence has emerged about the special characteristics of small firms and the need to adopt a different approach in management training (21). A number of the special aspects of smallness have already been mentioned, these include a lack of specialist management, lack of resources, the scope for personalized, owner-dominant management, short term, task specific focus and limited environmental impact.

As suggested by Gibb (22), personal and company objectives are often closely--interlinked and it is therefore difficult to distinguish between management development, personal development and organizational development needs. Without the training specialist resources possessed by the larger company, the owner-manager's perception of problems faced, may vary from externally diagnosed needs. Also, in not being able to fully identify actual needs, the owner-manager may need help from the trainer or fellow group members of a program to demonstrate linkages between organizational development - growth, survival, effectiveness etc with self development via a range of critical business skills.

To what extent then do owner-managers recognize the need to develop the organization's selling effort? The language of the 'ringing cash register' is well understood and this increases the receptivity of owner-managers to externally generated ideas to improve sales. Paradoxically the salesman role model is not seen with favor and, in the authors' experience, few owner-managers strive towards structured personal / management development to achieve better personal selling results. This point was discussed fully by the authors recently (23) and both causes and effects were contemplated within a UK / Irish perspective. A major cause was suggested to be the predominance of an 'employee culture' favoring the production or smooth operation rather than the demand creation so necessary to entrepreneurial success. The "good product will automatically sell itself" and significant negative selling stereotypes litter the authors' experience. Selling was not regarded as a respected management function but the home of 'smart talkers', 'conmen' or at best a breed of born, not made salespeople. However a contrary view is suggested by Brown (24): "in fact selling is a set of professional skills which individuals can develop, and this is particularly so in the kind of personalized selling which so often characterizes small firms".

AN ALTERNATIVE APPROACH

Experience over the past two years suggests that an alternative approach needs to be given to marketing training for the owner-manager. Such a revised approach was initiated in North East England by Cleveland County Council who requested a program that specifically concentrated on selling rather than broader based marketing issues. Their objective was to provide a specialized boost to recent starters and existing small businesses in an area where male unemployment rates approach 30%. Participants were expected to conform to a range of criteria identified by the Industrial Development Department. Most of them had or were about to receive small business grants and had already been given considerable counselling guidance and assistance. They were all well known by the industrial development section in terms of their financial, marketing and employment performance. Most had the potential and capacity to expand their business beyond a five - ten employee level or from a self-employment activity.

Since 1984 six programs have been completed, involving around sixty participants in a range of industrial, consumer and service marketing situations. No more then 25% had received any formal business education, let alone marketing training prior to the selling program. It is therefore worth exploring the rationale for elevating selling to appear before the introduction to formal marketing.

Despite considerable marketing inputs to small business programs, it is often surprising the limited impact these programs appear to have had on actual small business performance. Marketing thinking is perhaps deceptively simple in concept yet appears almost overwhelmingly complex in practice. Many of the models and concepts that have evolved in the marketing literature require a degree of sophistication and control that is beyond the owner-manager and inappropriate to his size of business. Furthermore in the small business case often the motivation as well as the understanding is lacking to facilitate the adoption of a more complex, sophisticated and disciplined method.

The revised approach recognizes that intervention must start at the perceived position held by the owner-manager. Most owner-managers understand the language of sales, even though performance in selling may be indifferent, marketing however requires a more fundamental and analytical approach to business management. The approach argues that training in selling techniques such as making appointments, handling objections, closing sales and prospecting can result in a more positive orientation to the market place rather than pushing general models and concepts at the owner manager. As selling is essentially a tactical area, results can be more immediate. Success can act as reinforcement. Then at the point in time when the owner-manager experiences improved selling, questions such as literature support, product range benefits and even competitive positioning may then be asked as a means of further improvement in sales. In short marketing, contrary to conventional wisdom, may emerge from successful tactical selling deployment. The acquisition of motivation, capability and resource may facilitate the need to revise marketing activity in a planned, commitment and integrated manner.

SALES TRAINING METHODOLOGY

A range of alternative sales training approaches have been used successfully by larger companies and training agencies for professional salesmen. A major choice is between a classroom or field based program. Field sales or on the job training is tutor intensive but rich in realism with direct feedback leading to simultaneous corrective coaching. Classroom training offers more control but could give rise to artificiality and questions of relevance.

Transferability of learning is a key requirement for small business training and to achieve this the programs we provided were a combination of classroom activity with personal action by participants in their own fields of selling. Each participant needs to digest a package of ideas and guide lines, try out its notions in the sales field, aid review his actions and associated learning back in the seminar.

The experience of the authors in methodological design and implementation has suggested a number of key considerations where owner managers are concerned.

--Programs need to be action based with a high degree of tutor / participant interaction to ensure understanding and review of skills and techniques.

--Emphasis needs to be placed on positive attitudina! development towards selling prior to encouraging skills development.

--Subject content may need to be sacrificed at times to ensure the transfer of a digestible amount of actionable points.

--To assist tutor / participant transfer a higher, but finely judged level of tutor ---> participant pressure than on other small business programs may be required. This 'pressure' may encourage more immediate action.

--By adapting an action learning group framework, peer group pressure may eventually replace tutor pressure.

--Strong visual images and role modelling assist the transfer of learning.

--Role playing has a key part to play in facilitating behavioral change in selling activity. Supported by CCTV and carefully designed situations, reflecting the real life position of each owner-manager, a new dimension is added to the learning experience. Role Playing is directly aimed at skills development and after a few seconds of self consciousness, the participants quickly fall into the spirit of the exercise and most benefit from it.

RESEARCH

Research was undertaken on the first four cohorts of owner-managers participating in action based selling programs in the North East of England. The main objective of the research was to establish post-program changes in performance in field selling actively and to establish owner- managers' perception of the relevance and impact of the formal learning experience. A number of methodological limitations were identified in the approach and these are outlined below. It was recognized that any conclusions drawn must be tentative and are not necessarily generalizable beyond the population surveyed.

A number of limitations were identified including:-

--the four cohorts were spread over a nine month period since the completion of the program. Therefore each participant had differing periods to implement new ideas and to change behavior.

--the selling situations and outcomes were likely to vary according to a range of economic/marketing variables such as competitive activity, growth, position in distribution channel, flexibility in product or process offering and in scope of operation.

--in the absence of any pre course appraisal of selling activity, assessment of program effectiveness needed to be based on participants' perceptions, and inferences drawn as to the contribution made by the training exposure.

A telephone questionnaire was administered to all participants who had completed the program. The questionnaire was designed to (a) assess owner-manager selling effort and performance (b) to identify key changes, as perceived by the owner-manager, since the programs completion and (c) to assess what, if any, changes had resulted from the training experience. A combination of five point Likert scales, multiple choice and open ended questions were used in the survey.

RESULTS

The telephone questionnaire generated thirty usable responses from a total population of thirty five participants. All of the owner-managers contacted had less than ten employees and most had been trading for less than three years. Responses can be grouped into five headings.

* Planning Sales Activity * Prospect - Customer Base Development * Initial Selling Approaches * Selling Skills * Overall Program Evaluation.

Planning Sales Activity

The authors hypothesized that an objective of the selling program was to ensure adequate time was allocated to the selling role, particularly because no other direct selling activity was likely. The immediacy and unpredictability of operational aspects may be overwhelming, giving rise to a fragmented, unsystematic and inadequate selling effort.

Nearly two thirds of participants spent less than 10% of their total working time in direct sales contact with customers and 86% spent less than 20%. In twelve cases some increase had taken place since the program, but the majority did not consider that this allocation had changed. As to be expected, a 'lack of time' and 'lack of staff' were given as the main reasons for no increases. It is worth contemplating whether this reflects the owner-managers' role or the priorities allocated to customer contact.

The responses indicated that the effort devoted to selling, in quantity at least, remained low. Although even professional sales personnel often only spend around 20% of their working time in direct customer contact, the balance of time may be utilized in critical pre and post sales support activity. There was little evidence to suggest that this depth of preparation existed with most respondents. It is interesting to note that 50% of respondents indicated that within the next two year period they predicted a greater personal involvement in selling at the expense of production. Aided by further production employees, these respondents clearly saw the need for additional effort to fuel sales expansion and saw this effort, most realistically coming from their own base of expertise.

Prospect/Customer Base Development

Although the size of each participant's customer base is likely to be influenced by both sector and scope of operations (subcontract manufacturing vs retail), questions were asked of the size and expansion rate in the customer base. The size of the regular customer base was below 15 for 64% of respondents and over 50% experienced some expansion in that base since the program's completion. However only four had experienced a significant increase during that time.

Perhaps the above findings are not surprising given the time allocated to selling efforts. Interestingly most respondents attributed the increase to a more effective selling approach rather than a raised level of general activity (i.e., number of calls, new prospects etc). Supporting questions were also asked of the methods used to expand the customer base with particular regard to prospecting. Referrals represented around 60% of respondents' main source of new prospects although 13 had introduced a formal prospecting record system utilizing such sources as trade directories, newspapers etc.

The responses suggested mixed outcomes from the program. Some participants desired expansion and took positive steps to achieve these objectives. Others were clearly content to operate within the confines of their existing base. The program, by discussing in some detail prospecting, had raised the issues associated with over dependency and stagnating customer bases. Some participants however were clearly not prepared to consider the need for sales expansion.

Initial Selling Approaches

A number of questions examined the need to gain access to buyers, especially in business to business selling. Most participants reported a need to maintain sales contact with regular visits and 16 out of 17 respondents normally made a prior appointment. When making appointments to visit new customers, 60% saw the 'cold-call' as the best method. Respondents were also asked whether their ability to make appointments had changed since the program. Some 92% of responses suggested a positive improvement with 30% highlighting a major improvement.

The problems associated with gaining access to industrial buyers are often underestimated. Although some organizations do have a policy of seeing at least once, a local supplier, in situations of entrenched competitors or non routine purchases some difficulty may be experienced by the novice seller. The responses indicated that by concentrating on specific techniques to obtain interviews, the owner-manager is better equipped to meet the obstacles encountered.

Selling Skills

Selling skills are often best assessed by direct observation rather than post event rationalization. However a number of questions were framed to establish the extent of preparation, problem searching, need identification and in overcoming customer resistance. An important part of the program was the demonstration of the need to structure and prepare for the sales presentation, particularly in the area of developing appropriate questions. Some 61% of the respondents reported that a prepared list of questions had been developed since the program.

Overcoming sales resistance by effectively handling objections, is a critical and necessary skill for any seller. Although nearly 90% of respondents indicated that their ability to handle objections had improved since the program nearly 80% were unable to be specific as to commonly met objections. Such a response was confusing. It could be that objections were not identified, as they were not so neatly 'packaged' as on the program or the range of objections was so varied that respondents found difficulty in identifying paramount factors.

Overall Program Evaluation

Readers will no doubt be aware of the problems of measuring and assessing the effectiveness of training. Part of the questionnaire sought essentially anecdotal feedback from participants on the perceived impact of the program on their selling activity. Of course it is recognized that caution must be exercised in evaluating subjective perspectives - the more people who say favorable things about the program the better! However because several months had passed since the completion of the program at least a more considered opinion may be obtained with the benefit of hindsight and subsequent experience in transferring learning.

Most participants considered the experience to have been worthwhile and highly appropriate to a new or recently started business. Although it might be argued that small business people are reticent in conceding that they have changed their attitudes, a significant minority of the group highlighted raised self confidence in approaching customers and a much more positive, as well as professional manner. It could be further argued that if such attitudinal change was valid, then the basis for deeper and more comprehensive training in selling and indeed marketing had been developed.

A significant number of participants commented on the value of role playing as a traumatic yet worthwhile experience, by providing an opportunity to test new ideas and techniques. A number sought follow up programs to develop their skills further.

CONCLUSION

The findings from this preliminary research, although not capable of wider generalization, suggest a need for further research and perhaps a re-examination of the contribution that sales training can make in owner-manager direct selling activity.

The emergence of action based programs, such as the selling course previously described, present an opportunity to provide immediate and short term benefits as an integrated part of the learning process. Further experimentation and reflection may consolidate the longer term contribution.

This paper suggests that training in selling can support a more effective exploitation of opportunities facing the owner-manager in the early years of operation. In a number of critical areas such as making appointments, prospecting, making presentations and demonstrations, overcoming customer concerns and handling competition, a significant number reported increased effectiveness. Given the limited time spent in direct customer contact with the pressures of performing a multifunctional role, the need for maximizing impact from limited contact was highlighted in this research.

As a result of the experience with owner-managers in the North East of England and Ireland, along with the tentative findings of this research, sales training may offer benefits to the participants over and above direct selling skills and techniques. A more positive orientation to the market place, an attitude change that both desires and is capable of achieving improved performance in sales may actually trigger higher levels of marketing thinking rather than result from it. If sales are lost through incomplete product ranges, poor supporting promotional material or inappropriate customer service levels, the owner-manager may actively seek, in a pro- active manner, solutions to perceived marketing problems. How refreshing and different such a position would be from that described by Carson (25) where the 'gospel' is often misunderstood, badly applied and rarely encompasses the totality of the business.

Sales Training is not another panacea. However by adopting an action-based, results orientated approach may actually facilitate a deeper and more fundamental change in the owner-manager who often needs, due to limited resources, to maintain direct personal contact with customers. Sales Training is not the only means of achieving such an orientation, other marketing tactical areas, especially closely related to short term results, may also assist. This paper is a small step in developing a greater awareness of the reason why marketing remains a problem in many small firms in the UK and Ireland and in suggesting an alternative approach to encourage increased performance.

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USING MARKET ANALYSIS INFORMATION FOR STRATEGIC DECISION-MAKING: AN EXAMPLE FROM THE TRANSPORTATION INDUSTRY

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ABSTRACT

This paper describes the results of a study of market analysis information for transportation services in a specific geographic location. The development of the sample and questionnaire are described. Information collected was used in strategic decision making regarding current and future services to be offered.

INTRODUCTION

Compiling market analysis information is only one component of a firm's strategic decision- making process, yet it is an extremely important one. The information provided by a market analysis can be useful to a firm since it aids in developing appropriate methods and processes of operation. Specifically, the information is helpful in profiling current market usage as well as identifying potential needs/ requirements of the market. This type of strategic planning is essential in allocating and using a firm's resources to achieve long-term objectives.

Over the last few years, the transportation industry has experienced deregulation and felt the impact of many environmental changes. As an illustration, increasing costs and a more competitive climate have combined to make it more difficult for small transportation companies to be profitable. During this period of change, trucking firms, for example, have experienced severe financial difficulties and a repositioning of the entire market as rails compete for a short-haul business. Due to rapid environmental changes, traditional competitive advantages of small carriers such as trucking, barge lines, and air have become cloudy. Price competition, energy costs, and new tax regulations all impact on profitability, market segmentation, and market share. Consequently, new strategies are necessary if small transportation companies are to survive in an era where even the large ones find profitability an illusive goal.

To obtain a better market perception of the transportation industry, market analysis studies need to be conducted to determine the changes that are taking place in various markets and to assist managers in making strategic decisions. This paper presents how a small transportation company can obtain market information and use the results for strategic decision making.

DESCRIPTION OF RESEARCH

The study presented in this paper was conducted by a group of college of business students for a regional transportation firm that has been in business for several years. The firm's name was not divulged during the collection of data, and the project was funded in part by the firm, the local Chamber of Commerce and a regional university.

The purposes of the study were to:

1. Provide a profile of transportation services currently used in the southwest Missouri area.

2. Identify potential shipping needs and requirements within the same region.

Ancillary questions in which answers were sought included:

--In light of the current era of deregulation and its more competitive environment, how are the problems and opportunities of freight transportation being met by transportation companies doing business in the southwest Missouri region?

--What transportation methods are used by manufacturing firms and why?

--How much and what types of freight are moved?

--Where are inbound shipments being sent from and what are the shipping points to where outbound goods are sent?

Development of Mailing List

The geographical area was defined as a 100-mile radius from Springfield, Missouri, which encompasses parts of Kansas, Oklahoma, and Arkansas as well as southwest Missouri. After identifying the counties included in this area, the cities within these counties were listed. Once the city names had been identified, the next task was to identify the business firms in these cities. Reference books, such as the Missouri Directory of Manufacturers, were consulted for a listing of all manufacturers within the targeted cities. Some large retailers were also included in the sample, the names of which were obtained from the Million Dollar Directory. The resulting list of approximately 1,000 businesses was cross-referenced against a customer list supplied by the participating transportation firm to eliminate duplications and defunct businesses and to update addresses. The final sample, narrowed by randomly selecting only one business from very small cities and two to three businesses from larger-size cities, totaled 373 firms. The development of the questionnaire mailed to this group is described next.

Development of Questionnaire

One of the primary objectives of the survey, as noted above, was to profile transportation services used by companies within the southwest Missouri region and to gain an insight into shipping needs and carrier selection criteria in the area.

Several sources were used to develop the survey. The questionnaire was reviewed by individuals in the transportation field and their suggestions for improving clarity and completeness were incorporated in it. The questionnaire is composed of 20 informational requests that are considered important for a transportation company to know in making strategic marketing decisions. Question 1 provides data to obtain a ranking of the relative importance of factors that may enter in to the carrier selection process.

Questions 2 and 3 deal with the present usage of carriers. Number 2 asks respondents to identify the various types of carriers now being used and the degree to which they are employed. Question 3 solicits a combined total of all carriers being used without regard to the extent of usage.

A dollar amount spent for inbound and outbound freight services is solicited in question 4. The responses here are important when they are compared to answers for question 17 (annual freight volume) and to question 20 (annual sales volume) in order to determine the role of freight expenditures in relation to freight volume and sales revenue.

Questions 5, 6, 7, 8, and 13 are designed to indicate the levels within organizations at which carrier selection and other shipping decisions are made as well as to determine the degree of stability in current shipper/carrier relationships.

Answers to questions 9, 10, and 11 provide an indication of shipper's needs from the standpoint of the type of freight being handled, its susceptibility to damage, and its packaging requirements.

The overall frequency of shipments and any seasonal fluctuation in frequency were addressed in question 12 while questions 14, 15, and 16 attempt to categorize freight volume into and out of the Springfield region in terms of principal markets, shipping corridors, and freight mileage per volume shipped.

The answers to questions 18 and 19, in conjunction with others such as question 11 provide insights into the service level required by shippers and the equipment demands to be expected by carriers.

Response Rate and Follow-up

In the early part of October, 373 surveys were mailed. By the end of the month 39 responses had been received for a response rate of 10.46 percent. Recognizing that this rate needed to be improved in terms of time frame to conduct the study, a telephone follow-up survey was implemented to see if the questionnaire had been received or if there were problems in answering it. For a number of reasons, it was discovered that many of the businesses had not received the survey. At this point, another 153 questionnaires were remailed to the same sample group, and by the middle of November, 50 additional responses had been received, for a response rate of 23.86 percent.

Results of Research

The total of 89 responses was coded and computerized. Descriptive statistics for each question were tabulated and are presented in Tables 1 through 7.

Table 1 contains information describing the criteria that respondents felt was important in choosing a carrier. Table 2 profiles transportation usage in the southwest Missouri area while Tables 3 through 6 present descriptive data on the forms and types of freight being shipped. Finally, Tables 7A and 7B show the top five origination and destination points for freight shipped to and from this region.

DISCUSSION

Several significant factors were evident after the results were evaluated. These factors are discussed as they relate to the purposes of the research. Considering the first purpose of profiling transportation services currently used in the southwest Missouri area, it appears that rail service is not heavily used and that most freight is being transported by common carriers --trucks-- and company-owned vehicles. Also, most respondents are currently using several carriers of all types. In addition, the respondents indicated a willingness to change carriers and to review what others had to offer. The total dollar amount currently being spent on freight, by a majority of the respondents, both inbound and outbound, is $50,000 and up. Although most of the freight being shipped was described as having low to medium susceptibility to damage, a larger percentage of outbound freight compared to inbound freight was described as having high susceptibility to damage. This fact seems logical since a large proportion of inbound freight comes in as raw materials and leaves as finished goods. The majority of both inbound and outbound freight is packed on pallets and in loose cases. Most inbound freight comes from the Midwest, Southeast, and Northwest. Outbound freight is shipped to the Midwest, Southwest, Southeast, and Northwest. Very little freight, either inbound or outbound, flows from or to the Northwest region. Finally, most inbound freight is LTL while outbound appears evenly divided between LTL and truckload.

In identifying potential shipping needs and requirements within the geographic area, respondents indicated that when they choose a carrier, they consider reliable pickup service, reliable transit, speed of transit, and cost as being important factors. Customer services and drivers are two additional factors that respondents identified as being very important. The respondents also require short-haul capability, frequent services, and service within the Midwest region. The descriptive characteristics of respondent's products (i.e. damage susceptibility, how freight is packed, description of commodities, and need for LTL or MTL capability) provided information regarding the type and extent of transportation service that respondents require.

CONCLUSION

The usefulness of the survey is not so much in what the results specifically show but in demonstrating the kind of information that can be collected rather easily and how a market analysis study can contribute very useful information for strategic decision making. For a transportation firm, the findings help profile transportation services being used in the region and are important in designing a market strategy and pricing structure. For the specific study presented here, the results helped the transportation company confirm some innovative strategies that were made in response to environmental changes. For example, service has become more flexible, reliable and, at the same time, maintains its cost advantages. In developing marketing strategies, small transportation firms have found that regional differences also compound the complexities of providing a common service to a large geographical area. Services used and required within a particular region can vary greatly and, consequently, even for the large firms it is not uncommon for a regional market to be quite different than what corporate headquarters perceives the company's overall market to be. As an illustration, railroads have the cost advantage in providing long distance movement of freight. However, one firm designed a train service that consisted of short trains -made up of flatcars hauling loaded highway trailers for relatively short distances.

In summary, strategic decisions should be made in light of environmental factors as well as internal organizational information. A market analysis study, similar to the one presented here, can contribute to the overall effectiveness of the strategic decision making process and the overall success of a small firm in meeting customer needs and long-range survival and growth objectives.

TABLE 1 CRITERIA FOR CHOOSING A CARRIER

Percentage of Respondents Who Viewed As Important and Very Important

Criteria Percentage

Reliable Pickup Service 93.3 Speed of Transit Time 92.9 Reliable Transit Time 92.0 Cost (Rates) 92.0 Carrier Coverage 80.5 Loss/Damage History 79.3 Pricing Flexibility 79.1 Quality of Customer Service 78.2 Claims Service 76.4 Quality of Drivers 76.1 Quality of Dispatcher 74.7 Completeness of Service 72.4 Financial Stability of Carrier 71.9 Familiarity With Carrier 69.1 Carrier Reputation 68.1 Quality of Sales Personnel 67.4 Loading/Unloading Facilities 64.4 Billing Service 63.2 Handling Capabilities 62.5 Domestic Distribution/ Consolidation Services 36.7 International Distribution/ Consolidation Services --

TABLE 2 PRESENT USAGE OF CARRIERS

Used > 25% Used 25%- Used < 75% Not Used Of Time 75% of Time Of Time

Company Owned 30% -- -- 25% Leased Trucks 58.9% 17.8% -- -- Common Carrier -- 25% 41% 34% Rail 55.4% 31.1% -- -- Air 28.8% 61.6% -- -- Other -- 53.4% -- --

TABLE 3A TOTAL DOLLAR AMOUNT PRESENTLY SPENT ON INBOUND FREIGHT SERVICES

Amount Percentage of Respondents

Under $5,000 10.5% $5,001-25,000 12.5% $25,000-50,000 10.4% Over $50,000 66.6% ------------ Total 100.0%

TABLE 3B TOTAL DOLLAR AMOUNT PRESENTLY SPENT ON OUTBOUND FREIGHT SERVICES

Amount Percentage of Respondents

Under $5,000 12.9% $5,001-25,000 15.4% $25,001-50,000 7.7% Over $50,000 64.0% ---------------- Total 100.0%

TABLE 4 SUSCEPTIBILITY OF FREIGHT TO DAMAGE

Percentage Response Inbound Outbound

Low 70.7% 49.4% Medium 31.3 31.6 High 3.7 19.0 --------------- -------------- Total 100.0% 100.0%

TABLE 5 WAYS FREIGHT IS PACKED

Percentage Response Inbound Outbound

Pallets 53.8% 48.2% Loose Cases 31.3 36.6 Bulk 11.2 8.2 --------------- ---------------- Total 100.0% 100.0%

TABLE 6 DESCRIPTION OF COMMODITIES

Percentage Response Inbound Outbound

Raw Materials 50.5% 13.2% Unfinished Soft Goods 15.2 11.6 Finished Soft Goods 5.1 18.8 Unfinished Hard Goods 6.3 7.2 Finished Hard Goods 12.7 27.5 Consumer Merchandise 7.6 15.9 Other 2.6 5.8 --------------- --------------- Total 100.0% 100.0%

TABLE 7A TOP FIVE ORIGINATION POINTS FOR INBOUND

Midwest Northeast Northwest Southeast Southwest

Position 1 67.1% 13.2% 2.5% -- 20.9% Position 2 56.0 -- 6.7 14.7 -- Position 3 57.7 -- 2.8 19.7 -- Position 4 56.7 17.9 3.0 -- -- Position 5 52.6 17.5 3.5 -- --

TABLE 7B TOP FIVE DESTINATION POINTS FOR OUTBOUND FREIGHT

	Midwest	Northeast	Northwest	Southeast	Southwest
Position 1	47.8%	--	1.5%	--	20.9%
Position 2	46.3	17.9%	--	--	17.9
Position 3	38.7	--	6.5	16.1	22.6
Position 4	45.8	--	--	16.9	22.0
Position 5	41.5	18.9	3.8	--	20.8