Three reasons that fostering entrepreneurship has limits

One of the mantras of modern economic development is that we must foster entrepreneurship. Luring businesses to relocate in a region has never been the whole answer. An area without an internal dynamic won’t thrive.

As a result, programs in entrepreneurship are everywhere: in high schools, community colleges and universities. And there’s no reason not to include entrepreneurship among the tools a region uses to invigorate its economy. But we need to be clear about the limitations of the approach.

After all, all tools have limitations. Improving the education and skills of a regional work force is a fantastic thing to do. But it takes a long time. Attracting new businesses can be wonderful as well. However, such efforts necessarily entangle a region in the controversial and frustrating game of targeted incentives.

What are the drawbacks of an entrepreneurship-led economic strategy? The first is that we appear to be botching the job already. The U.S. is becoming less, not more, entrepreneurial. The age distribution of businesses is rising, which means that the economy is increasingly weighted toward older, not younger, companies. There are fewer startup companies now (relative to the size of the economy) than a few decades ago. And startups are falling in greater numbers than ever before.

To a large degree, the rising failure rate is a function of persistent dysfunction in our financial markets. It is still tremendously difficult to get business loans, as banks continue to find other ways to make a profit.

A second limitation is that fostering entrepreneurship has a long gestation period. Perhaps that’s not surprising. The rate of technology start-ups, the kind we care most about due to their potential to create good-paying jobs, is correlated with educational attainment.

In other words, an area without a lot of college and grad-school degrees tends not to create a lot of technology companies. So if it takes a long time for educational improvements to take root, it makes sense that it would also take a long time before we see scads of tech startups.

Obviously, that’s a rather discouraging observation for a region like the Triad, in which the share of workers with a bachelor’s degree or higher is lower than the average for U.S. metro areas. For a region like ours, it may well be that we need to focus on low-tech startups instead of hoping for high-tech bonanzas.

A third limitation of the rush to entrepreneurship is that it has distributional implications. That is, entrepreneurship isn’t a ticket to the “1 percent.” Successful entrepreneurs are likely to be part of the 1 percent already. As with anything else, having resources and connections pays off, and the people with such assets tend not to be 99 percenters.

Consider the changing structure of Small Business Administration loans. SBA loans are guaranteed by the federal government, but the collateral requirements are more stringent than in the past. In effect, a borrower has to collateralize the entire loan, not just the unguaranteed portion. The result is that budding entrepreneurs have to decide whether to put up their homes as collateral. Not only does that discourage borrowing but it means that the people most able to benefit from the loan already have significant assets.

Nothing here is meant to suggest that we shouldn’t continue to find ways to help people start businesses. If anything, we need more of that than ever before. But given the obstacles in the path of entrepreneurial development, we need to be realistic about what it can do for us.