Comparative Patterns in Earnings and Economic Outcomes between Business Owners and Non-Business Owners: Findings from the National Longitudinal Survey of Youth

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Abstract

- Prior research using data from the National Longitudinal Survey of Youth 1979 Cohort (NLSY79) has found earnings patterns of young less-educated business owners are superior to earnings patterns of young less-educated wage and salary workers (Fairlie 2004).
- These findings suggest that business ownership and self-employment present a feasible pathway for less-educated and disadvantaged youths to escape poverty.
- Less studied is whether the earnings patterns of all business owners are superior to earnings patterns of wage and salary workers in general.
- **Beyond the psychic income that business owners receive from being their own boss, is it the case that business owners and wage-payers do better financially than wage-takers over the long run?**
- Prior research using NLSY79 data also shows that up to 2002, the mean and median earnings of self-employed men were meaningfully higher than earnings for men who were wage and salary earners, while the mean earning for self-employed women were meaningfully higher than earnings for women who were wage and salary earners (Fairlie 2005).
- **We build upon prior research by examining whether or not business-ownership in general provides a pathway to better economic outcomes over the long run.**

Introduction

- Empirical evidence that business owners achieve better economic outcomes than non-business owners over the long run may incentivize more potential business owners to follow their entrepreneurial instincts and start their own business.
- If better economic outcomes are associated with business ownership and if past is prologue, a higher startup rate and a greater share of the workforce that is self-employed should produce more aggregate wealth while also creating jobs.
- According to the Census Bureau's data set on Business Employment Dynamics, small businesses account for approximately two-thirds of the net new jobs created in the United States over the past two-and-a-half decades.
- Importance of the small business sector to the U.S. economy (from Small Business Administration Office of Advocacy):
- Small businesses make up 99.7 percent of U.S. employer firms and account for 48.5 percent of private sector employment and 46 percent of private sector output
- In 2011, there were 28.2 million small businesses and 17,700 firms with 500 employees or more

Data and Methods

- **Key methodological question: How to define a business owner given the data available?**
- The Current Population Survey (CPS) question concerning the "class of worker" category of the respondent lends itself as a useful tool to address this issue.
- Possible worker types include: (1) private sector employee, (2) government employee, (3) self-employed, (4) working without pay
- The CPS asks respondents to categorize their worker type for their (a) most recent job and, separately, (b) for up to five distinct jobs (labeled "Job 1," "Job 2," etc.), complicating the labeling of any particular individual as a business owner.
- Two approaches taken to define business owners using the "class of worker" category.
- **Approach 1**: Look only at respondent's answer to most recent job (*i.e.*, assume that the respondent's most recent job is the respondent's main job for a particular year) and ignore all other jobs for categorization purposes. Using this approach, a respondent is considered self-employed if they self-categorize their most recent job as a self-employed job (regardless of how many hours the respondent worked on average in their most recent job).
- A ***business owner*** using Approach 1 is defined as any respondent who self-classifies as anyone who self-identifies as self-employed in their most recent job for *any* five out of the ten "classification" years ("classification" years discussed in greater detail below).
- **Approach 2**: Analyze all five distinct jobs, categorizing a respondent as a business owner if for *any* particular job, the respondent self-classifies the job as a self-employed job *and* the respondent reports working at least 30 hours per week, on average, for that job. As with Approach 1, a business owner using Approach 2 is defined as any respondent who self-identifies as self-employed for *any* five out of the ten "classification" years.
- The ***classification years*** are years in which self-identification as being self-employed using Approach 1 or Approach 2 contributes toward determining whether a respondent is classified as a business owner (or not). Given the failure rate of new businesses (according to the SBA, approximately one-half of all establishments survive five years or more and approximately one-third survive ten years or more) and the phenomena of many entrepreneurs starting multiple businesses over the courses of their careers, a business owner defined using either approach need not self-identify as self-employed for five *consecutive* years.
- The classification years are the ten years spanning 1983 to 1992. The choice to begin the classification years in 1983 was influenced by the fact that 1983 marked the first year that all individuals in this cohort were at least 18 years of age (the 1979 cohort includes individuals who were 14 years of age when the surveys began in 1979).

Data and Methods (continued)

- The decision to limit the classification years to only ten years is arbitrary but was influenced by the length of the time series: The time series spans 34 years and we desired to observe economic outcomes 10 years and (nearly) 20 years from the end of the classification period.
- (Unweighted) sample sizes using Approach 1 and Approach 2:
- N = 294 (Approach 1), N = 0 (Approach 2)
- For obvious reasons, Approach 1 was selected as the classification method to define business owners. Weighted, the 294 subsample of individuals dubbed business owners constitute 3.5 percent of the total sample.
- Three indicators of economic wellbeing were analyzed for business owners and non-business owners: (1) total wage and salary income (of the respondent), (2) family net worth, and (3) total net family income.

Results

- Analysis of the economic wellbeing indicators show that business owners, as defined using Approach 1, clearly outperform non-business owners at both the (approximately) ten-year and 20-year mark (see **Table 1** below). These findings square with Fairlie's 2005 results, given in **Table 2**.

Table 1: Comparative Economic Performance between Business Owners and Non-Business Owners over Time: 1993-2012

	1993		2004		2008 (Family Net Worth) / 2012 (All Other Variables)	
	Business Owners	Non-Business Owners	Business Owners	Non-Business Owners	Business Owners	Non-Business Owners
Total Wage and Salary Income	$21,393	$19,865	$49,072	$38,084	$50,359	$46,723
Family Net Worth	$177,655	$58,778	$450,702	$236,609	$616,176	$322,560
Total Net Family Income	$49,935	$34,769	$91,401	$64,832	$82,273	$77,713

Note: NLSY79 family net worth data only extends through 2008. Total wage and salary income and total net family income data extend through 2012.

Results (continued)

Table 2: Results from Fairlie (2005)

	Men		Women	
	Self-Employed	Wage and Salary	Self-Employed	Wage and Salary
Mean	$52,300	$38,258	$28,217	$27,131
Median	$38,000	$33,021	$20,029	$23,407

Note: All figures given in 2002 dollars.

- Finally, the economic wellbeing for business owners and non-business owners was also analyzed by comparing the relative shares of each group in the top and bottom quintiles for each of the three economic indicators.
- That is, we answered the question: What share of business owners and non-business owners fell in the bottom 20 percent of aggregate total wage and salary income, family net worth, and total net family income, and what share fell in the top 20 percent (excluding records with zero values)?

Table 3: Share of Business Owners and Non-Business Owners in Top and Bottom Quintiles of Economic Performance Measures

		1993		2004		2008 (Family Net Worth) / 2012 (All Other Variables)	
		Business Owners	Non-Business Owners	Business Owners	Non-Business Owners	Business Owners	Non-Business Owners
Total Wage and Salary Income	Bottom Quintile	39.8%	46.0%	38.2%	48.1%	54.1%	49.9%
	Top Quintile	14.6%	6.3%	8.8%	3.9%	5.3%	3.5%
Family Net Worth	Bottom Quintile	55.9%	75.6%	51.7%	72.3%	56.3%	72.9%
	Top Quintile	7.0%	1.5%	8.0%	1.7%	8.9%	1.7%
Total Net Family Income	Bottom Quintile	33.7%	45.4%	37.4%	48.3%	48.9%	51.4%
	Top Quintile	14.6%	5.6%	10.7%	4.2%	4.3%	4.2%

Limitations

Most business owners do not launch their first business until around age 30. This being the case, the classification period potentially underestimates the amount of entrepreneurship occurring among the sample, as the sample in 1983 includes individuals as young as 18 years of age.

References

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