

Increasing Income Gap Threatens Small Business Growth

By Russ Smith and Esther Schlorholtz

There is an illusion of prosperity in Massachusetts that masks serious and increasing income disparities—these disparities are drying up personal income support for an important, if under-recognized, source of our economic strength: micro enterprises.

The middle class is shrinking—not by exiting out the top but by falling out the bottom. The incomes of 60 percent of our population have either stagnated or lost ground. These trends, if allowed to continue unchecked, will undermine our prosperity and decimate the many small businesses on which our local communities depend.

The Massachusetts Budget and Policy Center in its recent study, *The Growing Gap—Income Inequality in Massachusetts*, highlights the growing disparity in incomes in our state. In the last twenty years, adjusted for both inflation and tax policy, the top five percent have seen their real incomes increase by one hundred five percent, and the lowest twenty percent have seen their incomes rise by only sixteen percent. Moreover, in the past five years, middle class incomes have stagnated. High housing costs and rising health care and energy costs are making it even harder for people to cover their expenses.

For most of us this does not come as a startling revelation, rather it confirms what we already know—it is getting tougher to make ends meet in Massachusetts. Less evident is its impact on small business.

The Lowell Small Business Assistance Center, and others like it, have seen a dramatic fall-off in low- and middle-income people seeking assistance in starting small businesses. These very small businesses—from landscapers to child care providers, generally employing fewer than five people—are traditionally financed from savings, home equity loans or by friends and family. The increasing financial pressure upon middle and lower income families—with stagnant wages, soaring interest rates and increasing living costs—is drying up this important source of financing.

These businesses employ almost twenty percent of Massachusetts workers and support a payroll of \$4.6 billion. The impact, however, is more substantial than mere percentages would suggest. These businesses create neighborhood jobs, disproportionately employ first time, part-time workers and those educationally ill-equipped to compete in today's workplace. Yet because these businesses are small and financed outside traditional banking channels, they are simply not on the radar screen of economic development professionals. So there they quietly sit unknown, unstudied and largely unsupported.

These businesses are under capitalized and under resourced making them remarkably fragile and highly vulnerable to downturns in demand. The ratio of starts to closings is a thin 1.1:1 and it is

BOSTON PRIVATE BANK
& TRUST COMPANY

not unreasonable to assume that this sector of our economy is actually shrinking in the current market conditions.

There are things we can do to ensure that this critical sector of our economy grows. The Massachusetts Community & Banking Council (MCBC) works with banks and community organizations to create better and more accessible financing options. They also work with partners, including the state, to promote access to technical assistance for small businesses in order to improve the likelihood that businesses applying for financing will be successful. The passage of the recent Economic Stimulus Bill is making critical funding available to support small businesses and the technical assistance providers that support them. Much more needs to be done, particularly around the impact of business regulations and licensing to make it easier to do business in Massachusetts.

Current economic policy both nationally and locally embraces the assumption that “a rising tide floats all boats.” This presupposes that the prosperity generated is evenly distributed. Sadly, it is not. Right now, it seems that the rich are swimming with the tide; the middle class are caught in a rip tide and, at best, treading water while the poor have quietly drowned. We need to realize that long term prosperity is not based on a rush to the bottom but a true rising tide. We are, after all, ultimately in the same boat.

***Russ Smith** is the executive director of the Lowell Small Business Assistance Center that helps low-income people start small businesses as a path to self sufficiency. **Esther Schlorholtz** is senior vice president of Boston Private Bank and chairs the board of the Massachusetts Community & Banking Council.*

BOSTON PRIVATE BANK
& TRUST COMPANY