

Investigating the Dearth in New Venture Creation among Millennials

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Abstract

This literature based research explores the paradox of why the most educated generation in history, the Millennials, are creating fewer businesses than any previous generation. Several factors have led to the decline of new business creation among this age cohort. Research suggests that graduates are likely to work for established companies versus creating their own due to student debt burdens. The Millennial generation has flocked to higher education due to economic uncertainty and risk avoidance. One explanation of their economic conservatism is a psychological response to experiencing the Great Global Recession. Millennials pursue stability and exhibit low risk behavior in the labor market. A second explanation is market concentration and crony capitalism related to both government policy and market consolidation within industries. Policies that favor big businesses create difficult barriers to entry for entrepreneurs. Existing government policies favor larger firms and result in a competitive disadvantage for startups and small businesses.

1. Introduction

This research is to provide insight into why Millennials (20-36 years of age¹) are the most educated generation in history but their rate of business creation differs from any prior generation. The high demand for education in this generation is represented when considering that in 2013, 47% of this age cohort received a post-secondary degree.² An additional 18% are also more likely to attend graduate school than previous generations.³ Despite the growth in pursuing higher education, new business creation in the United States is at a 40-year low.⁴ Only 452,835 firms were incorporated in 2014, according to the most recent U.S. Census data released.⁵ That is well below the 500,000 to 600,000 new companies that were started every year from the late 1970s to the mid- 2000s.⁶ There are many contributing factors to this phenomenon. Student debt in the United States surpassed \$1 trillion at the end of 2014, making it the second largest household debt.⁷ Graduating with a large amount of debt is likely to hinder the ability/willingness to borrow money for business ventures. Another fact to consider is that the Millennial generation experienced the Global Great Recession during their youth, and as a result they sought higher education to prepare themselves for their future in the job market.⁸ Ultimately, weighing their opportunity costs, Millennials chose to take on the burden of student debt. This was to pursue stability and risk aversion in their future roles in the labor force. Another factor that is reducing business creation and increasing business failure is consolidation in the market. Economists argue a pervasive bias in favor of large corporations crept into government policy beginning about thirty-five years ago. Government policies that favor large corporations leave smaller businesses vulnerable to being excluded from competing in a fair market place.⁹ The barriers of entry into the market and the ability to compete have been directly affected by consolidation and crony capitalism.¹⁰ As consolidation grows, fewer firms can enter the market and stay sustainably competitive. Researchers provide implications of entrepreneurial intention in the future, comparatively to past generations.¹¹ They also provide explanations of why, despite the increase in education, fewer businesses have been created by this generation. The contributing factors to this phenomenon are: the effect of student

debt burden, conservatism due to economic uncertainty, and global market consolidation. The graphics provided from the U.S. Census Bureau depict this negative trend.¹²

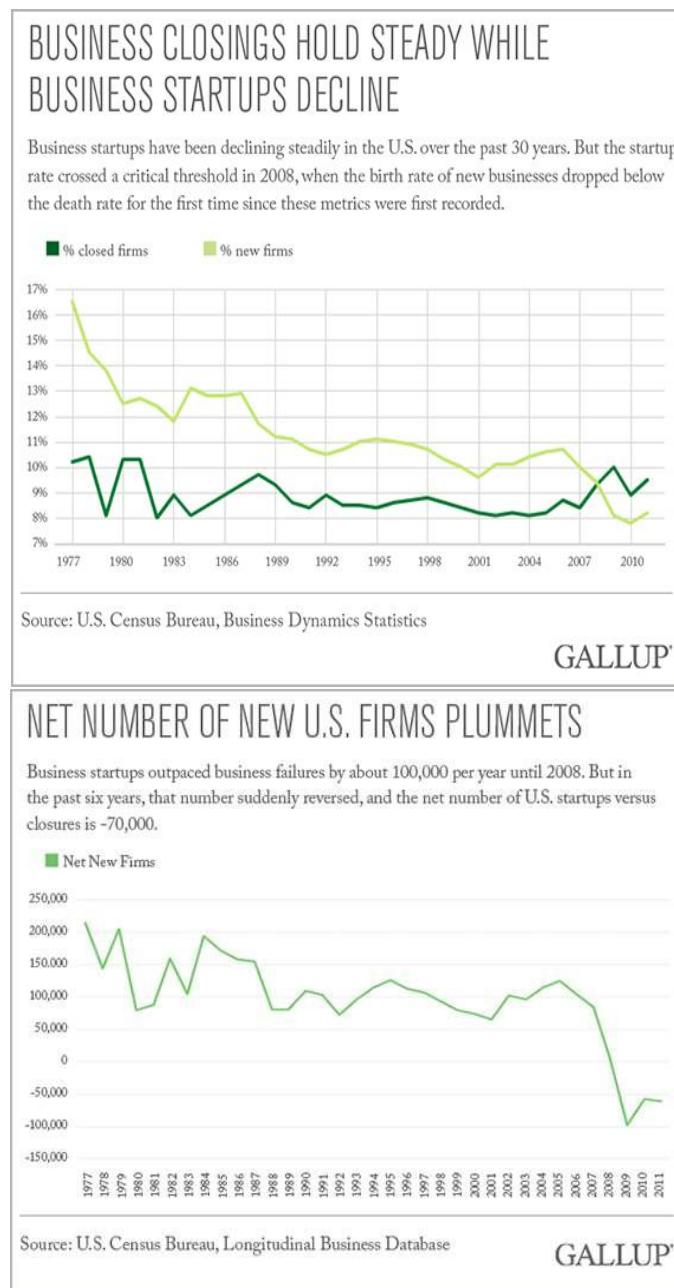


Figure 1. Business Closings Versus Business Start-ups

Figure 1. Demonstrates the decline in business creation in the United States in different age cohorts. It compares the decreasing number of start-ups and the number of business closures, showing how they are both in decline.

2. Higher Demand for Education and Associated Student Debt Burden

Fifteen years ago, only a handful of schools offered courses in entrepreneurship; today more than 1,500 colleges and universities offer some form of entrepreneurship training. There are currently more than 100 active university-based

entrepreneurship centers in the United States and more than 270 endowed positions in entrepreneurship, an increase of 120% in the past 5 years.¹³ The increase of supply is a result of the generations increase of demand for higher education in general. This results in not only the most educated generation in history, but also the most diverse.¹⁴ Accessing the cost/benefits of pursuing higher education is more difficult for some, as prices steadily increase and wages remain the same. Forbes founder Ewing Marion Kauffman recognized the need for students to complete a collegiate education, and that cost was a major hurdle toward that choice.¹⁵ It is only in the current environment of escalating college costs and student loan interest levels that scholars are becoming suspicious of a direct link between debt and entrepreneurship.¹⁶ The cost of higher education has been rising for decades, and the cost of in-state tuition and fees at public institutions have risen more than 50% in the past 10 years.¹⁷ This has increased the amount of debt students accumulate during their education. The re-payment of the loans that are expected upon graduation are difficult to pay when just entering the competitive labor force. Total student outstanding loan debt surpassed \$1 trillion by the end of the second quarter of 2014, making it the second largest category of household debt.¹⁸ With recent graduates carrying an average of \$35,000 in student debt, many would-be entrepreneurs are scared off from trying to turn their innovative ideas into a business.¹⁹ Student debt hinders innovation by forcing graduates to take the best-paying jobs they can find quickly to start paying off their loans, which impedes their ability to start their own endeavors. Besides making their hefty monthly payments, potential entrepreneurs also have difficulty securing loans for business creation due to their debt; the loan balance can bring down their credit scores significantly, making a loan through a traditional bank impossible.²⁰ These facts confirm that although higher education is more available to millennials, the debt-accrued does limit entrepreneurial activity. Individuals who experienced the Great Depression invested less and have pursued more conservative investing strategies throughout their lives.²¹ This suggests that the Great Recession will impact early savings and investment behavior among Millennials, but at this point, it is still too soon to know how large these impacts will be. According to the Federal Reserve Bank of New York, it may already have strangled their chances for success in the prime earning years of their lives.²² It is no secret that the rising cost of student debt is a growing national crisis; the latest numbers suggest that seven of ten college seniors last year graduated in debt. The total student loan burden in America today currently tops \$1.2 trillion, a number that has tripled in the last decade with interest rates of up to 12%.²³ This debt burden certainly places a life burden on millennials and with re-payment plans starting within six months prior to graduation, finding a job is a priority. Former President Barack Obama has said that a college degree has never been more valuable; however, if you borrow to finance your degree, the immediate returns are the lowest they have been in this generation.²⁴ The millennial generation is forced by their debt to seek gainful employment, instead of starting their own business ventures. Wages for the typical college graduate working full time have risen just 1.6% over the last 25 years, after adjusting for inflation; meanwhile, student debt burdens for the typical bachelor's degree recipient who borrowed for college have increased about 163.8%.²⁵ The impact of the student debt crisis among the Millennial generation is starting to show itself by the rising cost of earning a degree in the United States, and the student's inability to pay it off. It is important to consider that policy makers have contributed to this rise in the supply of education and ultimately contributed to the debt crisis surrounding borrowing money for school. Total student debt doubled during the Obama administration, with more than 90% of student debt either owned or guaranteed by the U.S. Department of Education.²⁶ Policy makers have incentivized Millennials to obtain higher education by providing an adequate supply and progressively making it more available through means of student loans. This not only presents a macroeconomic problem in the national economy, but also shows a significant microeconomic issue within new business creation. While Millennials are more educated than any previous generation, their earnings have not improved and their debt has increased— median annual earnings for Millennials in 2014 was \$35,000 which was equal to Baby Boomers.²⁷ Intuitively, a relationship between the two makes sense. Entrepreneurs need capital to start new businesses, and young people with student debt lag far behind on accumulating positive net worth today.

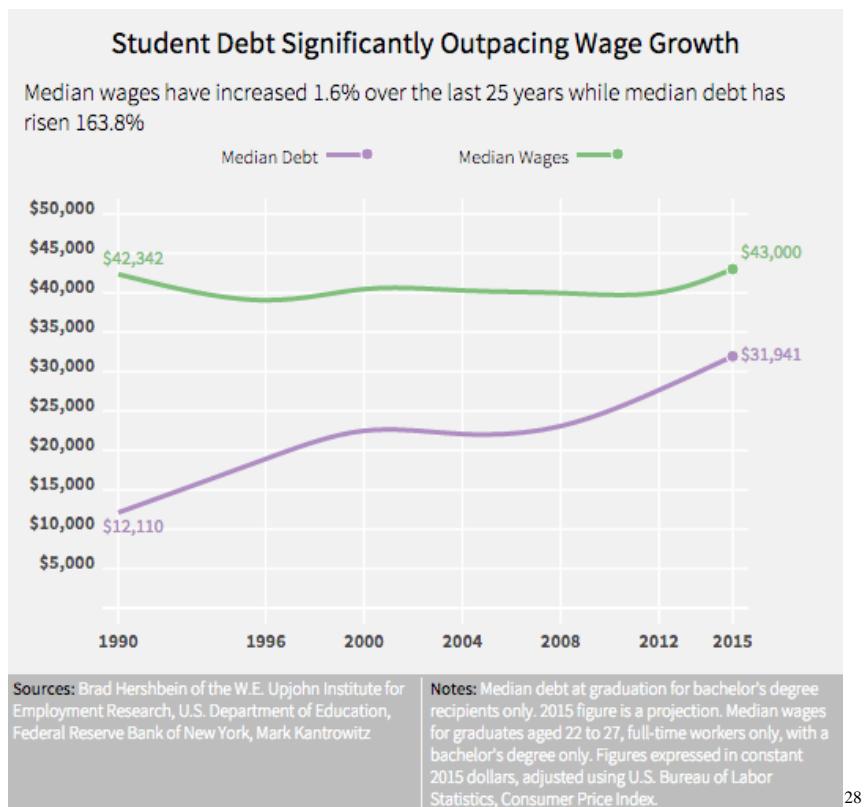


Figure 2. Student Debt Outpacing Wage Growth

Figure 2. This graphic shows how little median wages have grown in comparison to how dramatically student debt has risen; suggesting that student debt is hindering entrepreneurial activity in the Millennial generation.

3. Risk Aversion and Economic Uncertainty: The Impact of the Global Great Recession on the Millennial Generation.

After experiencing the Global Great Recession, the millennial generation turned to higher education to prepare themselves for their future in the job market.²⁹ Regarding the Recession, The Council of Economic Advisors of President Obama's administration noted, perhaps the most important marker for Millennials is that many of them have come of age during a very difficult time in our economy, as the oldest Millennials were just 27 years old when the recession began in December 2007.³⁰ As unemployment surged from 2007 to 2009, many Millennials struggled to find a hold in the labor market.³¹ Although the economy is well into its recovery, the recession still affects lives of Millennials and will likely continue to do so for years to come.³² Due to the uncertainty of the future job market and lack of trust in the economy, suggesting that millennials have invested more human capital through education than any prior generation. In 2013, 47% of 25 to 34-year-olds received a postsecondary degree (associates, bachelor's, or graduate degree) and an additional 18 percent had completed some postsecondary education.³³ Moreover, during recessions, young people tend to enroll in school in greater numbers and tend to stay in school longer.³⁴ This cyclical pattern reflects both a lower opportunity cost of schooling, as well as a stronger incentive to make one's skills competitive in a tough job market.³⁵ The economic perception by the millennial generation is centered in fear and distrust. Facts state that 23% of Millennials think they are "falling behind" economically, while 64% think they are "getting by" and mere 13% believe they are "getting ahead" economically.³⁶ Clearly, this generation is still feeling the slow burn of the Great Recession, paying for the collapse in missed investments, vanished trust, and lingering questions about the stability of our financial future.³⁷ So what does that mean for the future of entrepreneurs in the Millennial generation? It is suggested that the best way to help the Millennials trust the financial system again in the long term, is to build a financial system worth trusting.³⁸ Building trust within the economy is ideally the best way to push the Millennial generation into starting new business ventures and capitalizing on the supply of entrepreneurship

education. New research conducted by Hart Research Associates and Public Policy Polling on behalf of the Center for American Progress from 2013 to 2016 shows that Millennials' attitudes toward the economy have been shaped by the recession, with more Millennials citing economic stability as their top economic priority than any other goal.³⁹ This fact alone is enough to drive Millennials into the work force. Higher education and a "good" job will create the stability craved by an entire generation. Throughout their lifetime, Millennials' opinions have been influenced by laws and policies that have favored large corporations and the wealthy, but they still prioritize stability over prosperity.⁴⁰ The graph below illustrates the point that less firms are entering the market and more firms are exiting than in previous generations.⁴¹ This poses an economic issue because the willingness to start a business venture is a cornerstone of the United States economy and, while many millennials may want to be entrepreneurs, they have an economy that stands in their way.⁴² Economic Innovation Group co-founder, John Lettieri told the U.S. Senate Committee on Small Business and Entrepreneurship that "Millennials are on track to be the least entrepreneurial generation in history."⁴³ Although many Millennials admire startup founders and prefer self-employment, they're wary of starting businesses in an unforgiving economic environment. According to a study by the Small Business Administration, less than 2% of Millennials in 2014 were self-employed, compared with 7.6% of Generation Xers, and 8.3% of baby boomers.⁴⁴ This suggests that Millennials are failing to start businesses at an increasing rate. If this trend continues to increase, it creates greater challenges for future entrepreneurial endeavors, and will subsequently add to the issue of market concentration in the United States.

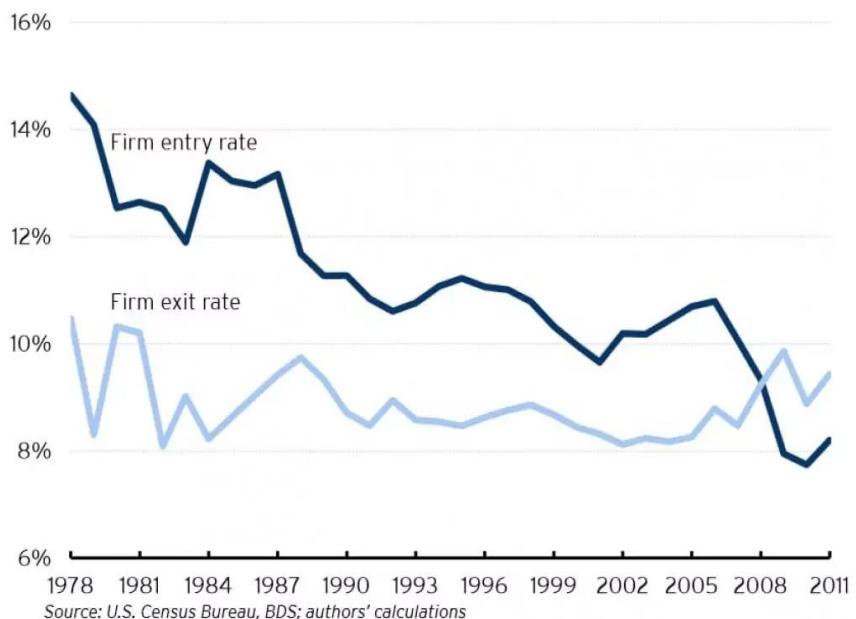


Figure 3. Firm Entry and Exit Rate Throughout Time

Figure 3. This graph shows the firm entry and exit rate in comparison to previous generations. Suggesting that firms' entry rates have decreased after the Great Global Recession and firm exit rates have spiked.

4. Market Concentration and the Challenges Small Businesses Face

Market concentration is related to both public policy and market power. Market concentration has changed the global market tremendously by creating more barriers of entry for small businesses. Information about Government policy is essential to visualize the problems related to fewer small business ventures among the most educated generation in history. Publications argue that this decline is to a significant extent, the result of a pervasive bias in favor of large corporations that crept into government policy beginning about thirty-five years ago.⁴⁵ The articles conclude that the changes in how the United States enforces anti-trust laws has left small businesses vulnerable to being excluded by

larger firms, excluding them from the competitive market, by sheer power.⁴⁶ The United States antitrust law is a collection of federal and state government laws that regulates the conduct and organization of business corporations, generally to promote fair competition for the benefit of consumers. Ideally, the market should flow freely and allow fair entry, but that's not reality for the Millennial generation. The truth is that big corporations and big government go together. The misuse of anti-trust laws has created an environment, where starting a new entrepreneurial venture appears to have become harder than ever. Although startups are central to Americans' self-image as a nation, especially in this high-tech age, new business creation has in fact declined sharply. The number of startups launched each year fell by nearly half between 1978 and 2011, according to a Brookings Institution study, and the decline has been picking up speed.⁴⁷ Business creation in today's market can be described simply in a few ways; For example, just two companies make 70% of our beer; one company processes more than one-third of U.S. milk; and four companies slaughter and process over 80% of U.S. beef.⁴⁸ In retail, Walmart now captures one of every four dollars that Americans spend on groceries, including more than half of grocery sales in forty metropolitan areas.⁴⁹ Online companies are reportedly more concentrated. Amazon, accounts for 35% of online sales in the United States and in 2015 they captured 51% of the growth in online spending.⁵⁰ The Millennial generation not only consumes from these market concentrations that are established in the United States, they also are forced to work in these industries.

US purchasing power: Top 4 customers represent >85% of retail market

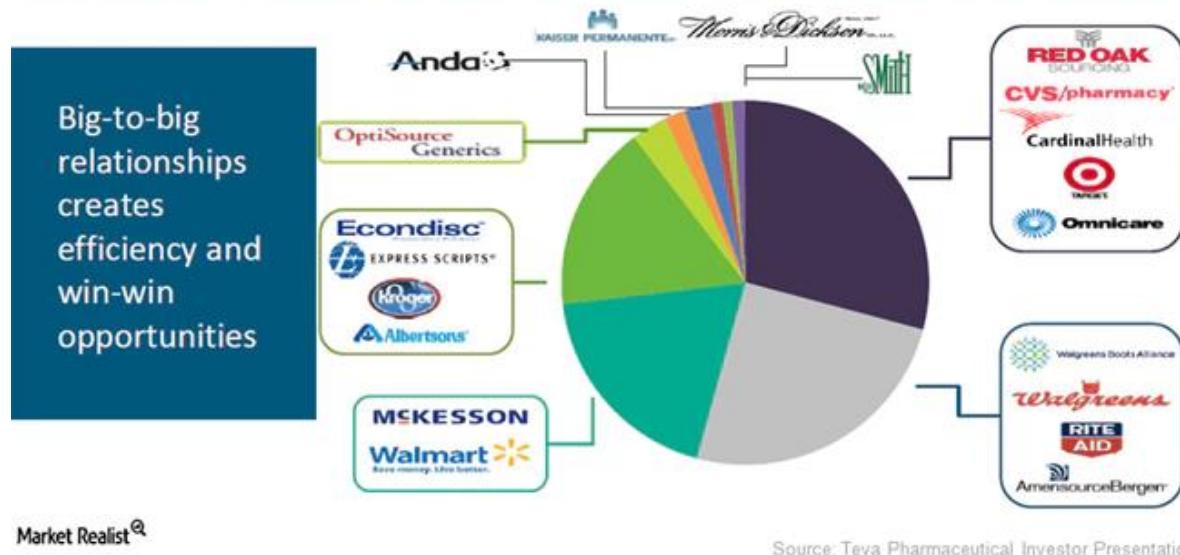


Figure 4. Market Power in the Retail Industry; A Representation of Industry Consolidation

Figure 4. This diagram shows some markets in the United States that depict consolidation within the United States. Confirming that market consolidation and market power play a role in the lack of new business creation and surviving in the market.

The research based upon consolidation in the United States suggests that new business ventures are less likely to survive in the long run. In a competitive market and the with amount of market power that is already established by firms, create an environment that excludes new business ventures from fairly competing. Four firms own 85% of retail market share⁵² in the generic marketplace today. This fact in general makes the argument about consolidation within the market as an obvious blockade to new business creation.

5. Conclusion

Considering some factors that have contributed to the Millennial generation taking on fewer entrepreneurial business endeavors, there are solutions that can be suggested to turn around this decline in activity. The first conclusion made from this research is the need to reduce student debt or implement student loan forgiveness programs that allow

graduates to pursue entrepreneurial endeavors instead of being forced to join the work force immediately. Related to this, the cost of tuition has increased over time, yet the wages paid to employees with higher education and skill sets have remained stagnant, regardless of inflation and the increased cost of living. The issues surrounding the student debt crisis could be addressed to open the door for the Millennial generation and help them engage in the creation of new businesses. The limitation that arises by students incurring so much debt before entering the work force could potentially be combated by providing incentives to Millennial entrepreneurs. For example, the government could provide incentives that motivate and encourage the students to pursue entrepreneurial endeavors upon graduation by making new business creation less risky. The government could use fiscal incentives and loan reduction policies upon completion of an undergraduate degree. Changes in policy could also be adjusted to instill the Millennial generation with more trust in the economy. Policy should recognize that entrepreneurship is a process, not a single act, and early education can be reformed to teach students the entrepreneurial mindset. Training future generations with the right skills and right attitudes to combat the psychological fears of starting a business and mistrust in the economy could be a good start to more new firms opening and surviving. The government could do more to break up monopolies and oligopolies in the United States. This relates directly to the problem of cronyism, and the fact that it is harmful to new business creation. Attention to the problems associated with crony capitalism in the market would not only allow more new business creation but could also increase the trust in the economic condition of the United States. This "pay to play" environment within the business world drives away business creation because entrepreneurs simply cannot compete in the market. Rebuilding trust in the economy could promote business creation by providing incentives for new businesses among Millennials and future generations. These suggestions could instill our national economy with an atmosphere that allows and encourages entrepreneurial activity.

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