Chairman Eduardo Garcia and members of the committee, thank you for the opportunity to submit comments about a crucial issue for California’s economic health.

The labor market is changing. The nature of work is changing. What is a job in this new economy? Who will create the jobs of the future? What do these changes mean for policy and economic developers today and in the future?

Contrary to popular belief and a disproportionate amount of attention, the foundation of the new economy is not going to be the 1% of the businesses that have the potential for high growth. Consider those companies as the skyscrapers. These businesses give shape to an economy much as a skyscraper provides a unique character to a cityscape. As most buildings in a city do not have dozens of floors, 99% of businesses will not grow to employ thousands, 88% of those will not grow past five employees.

The foundation of the new economy will be a strong infrastructure of many small, locally owned, diverse businesses. These very small businesses create all the jobs. The reality is that firms are starting smaller and staying smaller and that more people want to be their own boss. The Bureau of Labor statistics reported in March 2012 that the average size of new start-ups went from 7.6 employees in the 1990’s to 4.7 employees in 2011. The share of the self-employed in the labor market is growing exponentially (see graph below). The trend is expected to
continue. “Over the next five years we expect the number of Full-Time and Part-Time independent workers in America to grow by 25.4% to 37.9 million in 2020.”

Additionally, an estimated 7.6 million Americans will be regularly working as providers in the on-demand economy by 2020, more than doubling the current total of 3.2 million; and that workforce will grow by 18.5% a year for the next five years. (See attached report Intuit: On-Demand Workforce.)

Traditionally, economic development means redevelopment, enterprise zones, business attraction and tax credits. These efforts do not necessarily work. Most of the time they do not result in new net jobs, but result in a shuffling of the old and a loss of needed tax revenue. For example, nationwide business attraction strategies have resulted in a minimum of an $80 billion giveaway to corporations without much accountability. It is time to realize that businesses are not in business to create jobs, but to increase their bottom lines.

Business attraction, which has been our primary traditional economic development policy, is expensive. Nevada spent $1.25 billion in incentives to lure Tesla. That deal is projected to create 6,500 jobs – more than $192,000 a job, which is typical for business attraction. However, those job creation projections aren’t being met. According a study by the Nevada Governor’s Office of Economic Development, the project created 272 permanent jobs at the factory—representing a total quarterly payroll of $4.3 million in 2015. The projections were 700 permanent jobs with a total quarterly payroll of $40 million.
California should be thrilled that we saved the money. Instead, we recommend that the state invest half of the Tesla incentives, or $500 million, in local businesses assistance. At a cost of $5,000 a business, that would create 50,000 business owners.

A shift is needed to move from old methods that may have worked for a different economy to a new innovative, creative and flexible method that will work for today’s economy – a method that is based on creating jobs in California, one based on a “Do-It-Yourself economy”.

The D-I-Y economy is a natural extension to the growing D-I-Y and maker movement. Instead of remodeling your own home or creating your own solar powered radio, the D-I-Y economy is “about driving economic development at the local level, with local leadership, guided by a more robust and sustainable vision.”

California needs a strategy that will harness our state's entrepreneurial spirit to create new businesses and grow new jobs by cultivating homegrown local businesses. Rather than investing our scarce resources in attracting businesses from other states or by underwriting expansion of large corporations through tax breaks, California can tap its indigenous entrepreneurial resources, using existing programs and funding sources.

Five different components make up the D-I-Y ecosystem, the five ‘C’s: Coaching/training, Capital, Connections, Community, and Culture. When the pieces are in place, local economies can foster independents and micro-business owners and create a sustainable, self-reliant, and thriving local economy. The rest of this written testimony dives into each of the five ‘C’ in detail and makes suggestions on actions the state can take.

**FIVE ‘C’s of a D-I-Y ECONOMY ECOSYSTEM**

**COACHING** - Scale up business technical assistance for microbusinesses and gazelles (high growth potential businesses)

Business assistance is the first step in the capital access process and the first step to success for locally grown small and microbusinesses. Think solid business plan, robust cash flow statements, marketing plan. A business has to have its proverbial ducks in a row in order to be creditworthy, and then they can apply for a loan and grow.

The Aspen Institute FIELD studies show that businesses that receive assistance have an 80 percent success rate as compared with the 50
percent to 80 percent mortality rate for small businesses overall that the Small Business Administration (SBA) cites. On average, they create two jobs in addition to their own over a three-to-five year period.

For example, Jose and Rosie Rodriguez own King City Tires in the southern Salinas Valley in California. Their region is very distressed with an official unemployment rate of over 16 percent and a real rate closer to 30 percent. King City Tires found a niche servicing tractors in the fields, 24/7. It took two years of business counseling from El Pajaro Community Development Corporation for the Rodriguez' to qualify for a $1.5 million Small Business Administration loan to expand their business. Now they employ 16 full-time workers (see photo.)

El Pajaro CDC is one of 85 CAMEO member organizations in California that provide business training, technical assistance and financing to entrepreneurs. Yearly, these organizations serve about 20,000 very small businesses with training, business and credit assistance and loans. These firms -- largely start-ups with less than five employees -- support or create about 35,000 new jobs in California.

The business assistance programs include Small Business Development Centers (SBDC), Women's Business Centers (WBC), non-profit entrepreneurial training organizations and non-profit lenders. They provide low-cost and quality assistance to business owners of all stripes.

These organizations should be supported and promoted by state and local governments. Traditionally, they have been funded by U.S. Department of Housing and Urban Development's Community Development Block Grant funding, the SBA, USDA, and corporate contributions. Many have seen these funds systematically cut back, particularly in rural regions, whose business development organizations have reduced the numbers of businesses that they are able to serve.

What the state can do

State and local governments concerned about local economic development should invest in business assistance programs. For example, they could provide a match to the federal grants. The Governor could use discretionary Workforce funds to incorporate entrepreneurship training into the system as a demonstration project.
The 2014-2015 and 2015--2016 California state budgets include $2 million for a Capital Infusion Program overseen by the Office of the Small Business Advocate. The money is competitive grand funding to the California Small Business Development Center (SBDC) Networks to expand help them attain loans, investor capital, understand and resolve their credit readiness issues and develop funding strategies for business expansion or startup.

According to their annual report, in fiscal year 2014-15, 34 SBDCs across California received grant funds. In fiscal year 2015-16, 41 centers received funds. In the first year of the program, the Capital Infusion Program resulted in more than $200 million in documented capital infusion, exceeding the program’s goal by more than 50%. That is a hefty 1-100 ROI! With such a great ROI, it only makes sense to increase funding and expand this program to other business assistance organizations.

A strong microbusiness infrastructure will ensure that business owners receive coaching so that they can be part of the 80% that succeed (and not the 80% that fail.)

**CAPITAL**

Despite their crucial role in the economy, only 0.10% of potential microbusiness borrowers is being served in California. Many polls find that small business owners believe the availability of credit is a problem. Larger banks are making fewer loans under $250,000, because they can do the same amount of work and earn more money with larger loans. Alternative lending sources, e.g. community development financial institutions (CDFIs) and community banks, are a good source of capital for small businesses. CDFIs are non-bank, non-profit lending organizations and credit unions that support business development and provide personal business loans in local communities that usually are underserved by traditional banks.

Small loans mean a lot. A research paper, How Much Does Credit Matter for Small Business Success in the United States?, compared similar potential borrowers except for whether they received a loan or not. Applicants who receive a loan

- are 54% more likely to qualify for future business loans;
- are 54% more likely to survive; and
- increase their sales by an average of 41%. 
CDFI's offer loans ranging from microloans (under $50,000) to $250,000. Many CDFIs provide small-business coaching and other professional resources, such as legal, accounting, and marketing assistance, to grow their borrowers’ small businesses. CDFIs usually have more flexible lending criteria than traditional banks. Businesses do need to show the ability to pay back the loan through positive cash flows and have a business plan. The loan criteria is often listed on the lender's website and vary in terms of a business location, loan size, interest rates, risk, borrower income, etc. CAMEO's 28 member lenders made 3,000 microloans in 2014.

*One note of caution:* Technology has also created a flood of online business lending companies. The biggest online lending segment for small business loans are not loans at all, they are Merchant Cash Advances (MCA). MCAs outweigh other lending by a factor of six. Often MCAs are high-cost and short-term and can easily put a small business into bankruptcy. As merchant cash advance companies are not technically lenders, they are not regulated.

One of CAMEO's board members has called Merchant Cash Advances more destructive than terrorists, because of the extent of the damage that they can do is more common and widespread than terrorism attacks.

Navigating the space is challenging, even for an experienced borrower. Rates, loan structures, fees, terms, etc. can be hard to discern from the websites. While many of these lenders offer quick turn-around, they are often expensive and can hurt the bottom line. A borrower should thoroughly understand the loan terms before taking out a loan with an online lender.

*What the state can do*

Loans to small businesses that do not have credit history or do not have bank-worthy credit, is riskier than many lenders would like. The state could help increase access to capital and expand loan guarantees for CDFI lenders.

The state could also educate small business borrowers on what a responsible small business loans looks like and what to be wary of when looking for access to capital.

Right before the end of 2015, California's Department of Business Oversight sent (DBO) “an online survey to 14 marketplace lenders requesting five-year trend data about their loan and investor funding programs.” The answers were due March 9, 2016. This is a good step and
we hope that DBO issues their findings in a timely manner. We urge the state to go further and push for federal regulations or implement them on their own.

CONNECTIONS to Markets

A business can have a great idea, a great plan, and money to implement the plan, but without clients or customers, there is no business. In order to thrive and grow, small businesses need **connections to market opportunities**.

Examples of approaches that economic developers can take to increase connections to markets for their businesses include:

- Support for online platforms that provide direct links to customers and break down barriers to entry and/or provide marketplaces for goods and services;
- Implementation of local procurement programs;
- Use 'economic gardening' to connect local businesses with market research and business opportunities; and/or
- Inventory local needs and resources to determine the innate market strengths of the local economy and determine what is missing to help it grow.

Online platforms run the gamut of industries – from hotel rooms (AirBnB) and taxis (Lyft, Uber) to retail (Etsy) and services (Thumbtack). These platforms enable households to augment their wage income, as well as create client-bases for businesses. One struggling IT repair shop owner signed up for the Thumbtack platform at the suggestion of his lender and found five new clients in one week, more than he had in the last three months. In Santa Cruz, Barbara Mason has supported hundreds of Etsy businesses with training and peer group meet-ups.

Procurement policies that encourage governments to source locally have great potential to grow their local economies. **Locally owned firms’ revenues recycle in the economy three times the rate as national firms through the multiplier effect.** Between 2006 and 2007, the State of California generated **50% more economic activity** (an estimated $4.2 billion in GSP and 26,000 new jobs) when it contracted with disabled veteran-owned businesses and local small businesses instead of larger companies. A meaningful shift of government spending toward local businesses can impact the local economy in a significant way.
**Economic gardening** initiatives provide local entrepreneurs with access to competitive intelligence on markets, customers and competitors that is comparable to the resources customarily only available to large firms. Local economic development teams can aggregate small businesses onto a market research platform. One such tool is [SizeUp LBI](http://www.sizeup.com). It’s an online tool that helps small businesses benchmark themselves against the competition, identify potential customers, suppliers and competitors; locate the best areas to advertise; and research demographics, consumer spending and labor force for their unique business location.

**Regional industry clusters** are synergistic concentrations of firms and related networks. A great is example is the value chain developed by the USDA California Rural Development Office. The USDA convened the players and stakeholders in four regions, determined existing resources and helped to fill the gaps. This process discovered that California ranchers ship cattle out of state for slaughter and cold storage was scarce. Two mini-industries were born: mobile slaughterhouses for getting local grass fed beef processed to meet local demand and cold storage facilities to save on increasing energy prices. The region can be defined as needed – neighborhood, city, county, several counties. Margo Prado has undertaken a similar effort in Oakland, in which she has examined the city’s small manufacturing industry to determine who makes what for whom and how she can link local suppliers with local buyers.

Local businesses are a key constituency in your community. If you help all of your local businesses, especially the small ones, you will see job growth and economic success for your community.

**What the state can do**

Procurement policies that encourage governments to source locally have great potential to grow their local economies. As mentioned before, a meaningful shift of government spending toward local businesses can impact the local economy significantly.

The more that California and municipal governments invest in self-employment and the entrepreneurial ecosystem, the stronger that California’s communities and collective economy will be.

**CLIMATE**

It is a misconception that small businesses are anti-government. However, most often large corporations exert more influence in the policy arena than small businesses, often resulting in government regulations
and policies that favor larger businesses over smaller ones. Of course small businesses are interested in a strong infrastructure, (e.g. good roads, reliable broadband), the ability to compete with the large businesses, and increasing the demand for their products. However, a positive regulatory approach that promotes the DIY Economy would benefit small businesses of all sizes. The approach means investing and supporting self-employment and the entrepreneurial ecosystem that we have been talking about in the rest of the series, i.e. coaching, capital, and connections.

**What the state can do**

In addition to the policy efforts described about, California can support self-employment.

Self-employment needs to be recognized as a job creation strategy that works for cities and states, both urban and rural. CAMEO has led the effort to initiate systems change within the Workforce System to permanently adopt and integrate self-employment training for the unemployed. In 2010, the Department of Labor (DOL) released directives encouraging the local Workforce Investment Boards (WIBs) to integrate entrepreneurial training as a vital workforce development strategy - **TEGL-12-10: Supporting Entrepreneurship and Self-Employment Training through the Workforce Investment System**. We expect DOL to issue performance measures within the new WIOA soon, which will enable entrepreneurship to be integrated effectively at the local level. The California Department of Labor should ensure that self-employment performance measures are defined.

The State Workforce Investment Board (WIB) should encourage local WIBs to carve out 5% of their Workforce Investment Act (WIA) funding from the Department of Labor (DOL) to help the unemployed become self-employed.\(^1\)

The Governor should give incentives to local WIBs to partner with the 100 Micro Enterprise development organizations and Small Business Development Centers that offer the training and technical assistance that new entrepreneurs need to succeed. Money could come from discretionary funds or new DOL Workforce Innovation Funds as available.

Staff training is another key to integration of self-employment opportunities into the workforce system. CAMEO developed a training module –

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1 DOL report estimates that 5% of unemployed could be self-employed with appropriate training and support. In California this comes to 120,000 potential entrepreneurs. If just 40% are successful, 48,000 new businesses would start and create jobs.
“Understanding Entrepreneurship” - that provides a substantive orientation to entrepreneurship training and business assistance services for economic development and workforce professionals who are responsible for assessments and referrals of persons likely to succeed in self-employment. In partnership with the California Workforce Association, we held three “Understanding Entrepreneurship” workshops for fourteen WIBs in the Central Coast, Sacramento and Redding.

Resurrect the Self-Employment Assistance (SEA) Program: Under the SEA program, unemployed workers will be able to receive or maintain their unemployment insurance benefits while they start their own small businesses.

CULTURE

The final ‘C’ is the culture of entrepreneurship, something for which California is known. We have lots of entrepreneurial energy in this state at all levels, and not only in the high technology sector. We re-invented the roach coach into an entire food truck culture/phenomenon/$1 billion business. When we refer to entrepreneurs, we refer to all entrepreneurs – from the tamales lady to the soap maker to the local grocery store owner to the veterinarian to the app developer to the medical device inventor.

What the state can do

Elected leaders can promote this new direction throughout the state. For example, the Governor or legislative officials could

- Hold a conference to show case effective programs and solutions and encourage agencies to make incentives available to cities and counties to implement a California-grown economy.
- Convene major financial institutions, corporations and foundations to support this new direction by increasing investments in the small and microbusiness sector.

CAMEO would like to thank the JEDE committee for giving us the opportunity to share our views.