

# Democratizing Globalization:

How Small Businesses across America  
are Growing in the Digital Marketplace

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# Executive Summary

Across the United States, vast numbers of people, maybe more than we previously realized, have not benefited fully from globalization. The high capital, infrastructure, and communications costs associated with the global marketplace meant that only the largest businesses in the country could fully reap the benefits of trade. Moreover, businesses that saw the gains from globalization were concentrated in large city centers, often close to the coastline, in order to reduce the distance costs associated with trade. The Internet changes the calculus of who can fully engage in globalization by eliminating traditional barriers like distance, trust, and communication. Breaking down these barriers can enable businesses outside major cities and those located on the coasts to reap the economic benefits of an open economy.

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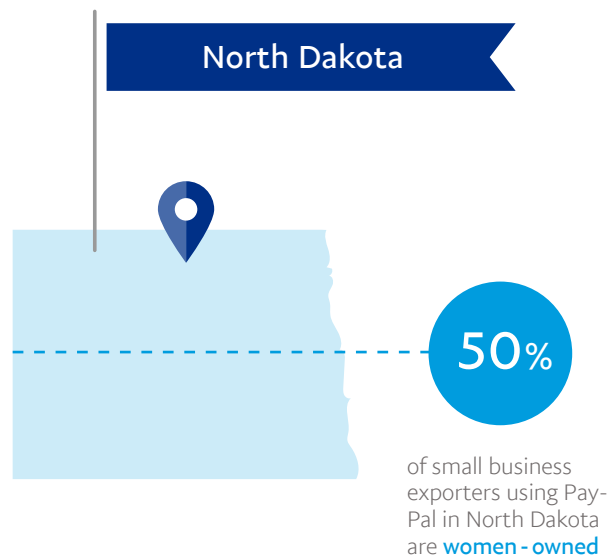
Pioneering research done by eBay in 2012 demonstrated that even the smallest retail business could now go on the eBay platform and sell physical products around the world. This paper builds upon the research done at eBay demonstrating that the benefits of digital are not limited to a sole platform or business model. This study looks at the impact of the Internet on small businesses in nearly every sector, in every part of the country.

We have analyzed a sample dataset of over 29,699 small businesses using PayPal across the United States for a one-year pe-

riod from 2015 and 2016. We did a robustness check using a broader dataset of over 100,000 small businesses. We define small businesses in the PayPal dataset as those selling between \$30,000 and \$3 million per year. We found that small businesses that used PayPal demonstrate growth and exporting trends that are significantly different from traditional small businesses.

## Here are the most noteworthy findings from our research:

- Small businesses that used PayPal grew. From 2015 to 2016, small businesses on PayPal grew 22.9% year over year. In comparison, US small businesses (businesses with less than \$5 million in annual revenue) grew 7.8% from 2014 to 2015, the closest comparison metric available.
- Small businesses that used PayPal were far more likely to export than the traditional small business. Less than 5% of all US small business export. On PayPal, 79% of small businesses analyzed exported.
- Small businesses using PayPal that exported exhibited enhanced growth. Small business exporters on PayPal grew 32.8% from 2015-2016 (compared to 22.9% growth for small business generally).
- Small businesses in nearly every sector exported using PayPal. Trade by businesses in service sectors (including education, health care, administrative services) was previously considered impossible, but we found that the small businesses from service sectors that use PayPal are now just as likely to trade as manufacturers or retail small businesses.
- Women-owned small businesses that use PayPal grew and exported. 72% of women-owned small businesses on PayPal exported. These women-owned small businesses can be found all around the country. The number of women-owned small business in ND was particularly notable as 54% of small business exporters that used PayPal in North Dakota were women-owned. The average growth rate for women-owned businesses on PayPal is nearly a mirror image of the growth rate for businesses owned by men.
- Small businesses in the heartland of America grew and exported using PayPal. Small businesses in the heartland of the US (defined as those businesses not on the coasts) were almost just as likely to export (80% of coastal merchants exported in both 2015 and 2016, compared with 78% of heartland merchants) and heartland exporters had slightly higher growth rates than those located on the coasts (32.1% for coastal and 33.6% for heartland).
- Small businesses in rural towns (less than 50,000 people and not in an Urban Area as defined by the US Census Bureau) were just as likely to export as businesses in urban areas and had similar growth rates.



These numbers seem to turn conventional thinking on small business growth and trade on its head. Our data shows: Small businesses no longer need to grow to a certain size before they begin to trade; small businesses no longer need to focus on a specific sector to engage in trade; and small businesses no longer need to move to coastal areas or large city centers to grow. The Internet opens up a world of possibilities for entrepreneurs and small businesses to thrive in a way that was never before possible.

Despite the equality of opportunity provided by the Internet there remain inequities that prevent small businesses in the US from achieving their full potential. Policymakers have a role to play in creating an enabling environment for small businesses using the Internet.

We recommend that policymakers focus on the following four areas, as they correspond well to the barriers that small businesses face:

### 1 Access to Finance

Has always been one of the major barriers to small business growth. Digital tools are enabling new forms of underwriting that is expanding capital access; policymakers must be weary when regulating these new forms of growth capital.

### 2 Licensing

The Internet now enables a service provider to sell services around the world, but licensing regimes exist in many service sectors [ie. legal, education, medical]; policymakers should look to passporting regimes that enable professionals to legally offer services across borders.

### 3 Customs and Duties

When small business retailers export they can often struggle with complex customs and duties requirements; policymakers should push for exemption from customs and duties for low value transactions.

### 4 Digital Education

The Internet does provide equality of opportunity, but only for those that know how to take advantage of it; government small business training programs must be adjusted to focus on digital tools and services that can help business grow.

If we get these four areas of policy right, we can unlock additional growth opportunities for small businesses in the US. Healthy small businesses means healthier community economies, which means a healthier economy overall.

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*At PayPal, we are dedicated to democratizing financial services. We want to see every small business in the US grow by using the Internet to take their product or service to customers around the world.*

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We hope that this research inspires new thinking around small business development and spurs policymakers to think about how they can best support growth for small businesses across the US.



# 1. Introduction

Small businesses are the lynchpin of the US economy. Small businesses employ over 55 million Americans and are responsible for the vast majority of net new job creation. Small business growth not only leads to increased jobs, but it also leads to healthier community economics and a more stable overall economy.

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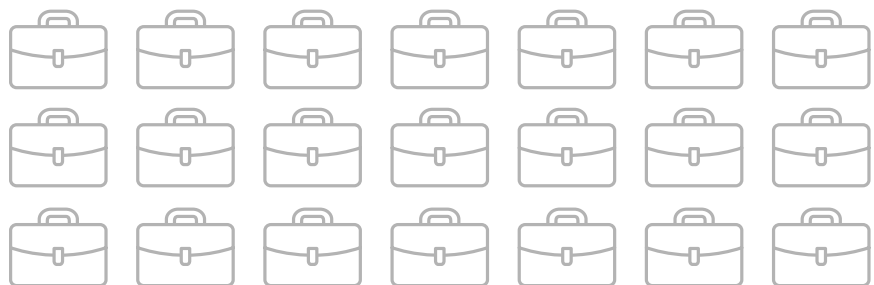
Small businesses have been growing at a steady rate in the US since the financial crisis, but small business sentiment continues to be well below what it was in the 1990s. Moreover, the growth of small businesses in recent years has largely been limited to those located in major city centers. Small businesses in rural and suburban towns across America had been setup to support the industrialization of the 20th century, and have struggled in recent years due to shifts in the economy. Cities have built infrastructure, a strong labor pool, and created incentives to attract small businesses and entrepreneurs. Rural and suburban towns have struggled to keep up.

Moreover, globalization has changed the landscape for small businesses. Globalization enables businesses to enjoy greater revenue and profits through a larger customer base and an enhanced supply chain. But, small businesses have not traditionally been able to take advantage of globalization due to the high upfront investment costs in building infrastructure and relationships.

**55** Million

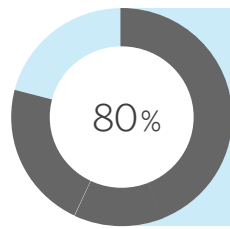
Small businesses employ over 55 million Americans.

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## US Economy:

Small businesses  
in the services sector



Businesses located on the coasts were more likely to benefit from globalization as they had lower “distance costs” to acquire customers or build business relationships in foreign countries. And, businesses in large cities were more likely to trade as they were able to develop contacts and engender trust across borders in a manner that rural and suburban small businesses struggled to do.

The Internet has turned the traditional story about small businesses and globalization on its head. Small businesses that have struggled to grow since the financial crisis are finding new opportunities online. Pioneering research done by eBay demonstrated that the traditional distance costs limiting small businesses from trading have largely been eliminated. The services built on top of the Internet can generate leads, engender trust, and enable safe and efficient financial transactions across borders.

*Services like accounting, design, or other personal services have traditionally been impossible to trade as they required a physical in person engagement in order to be delivered.*

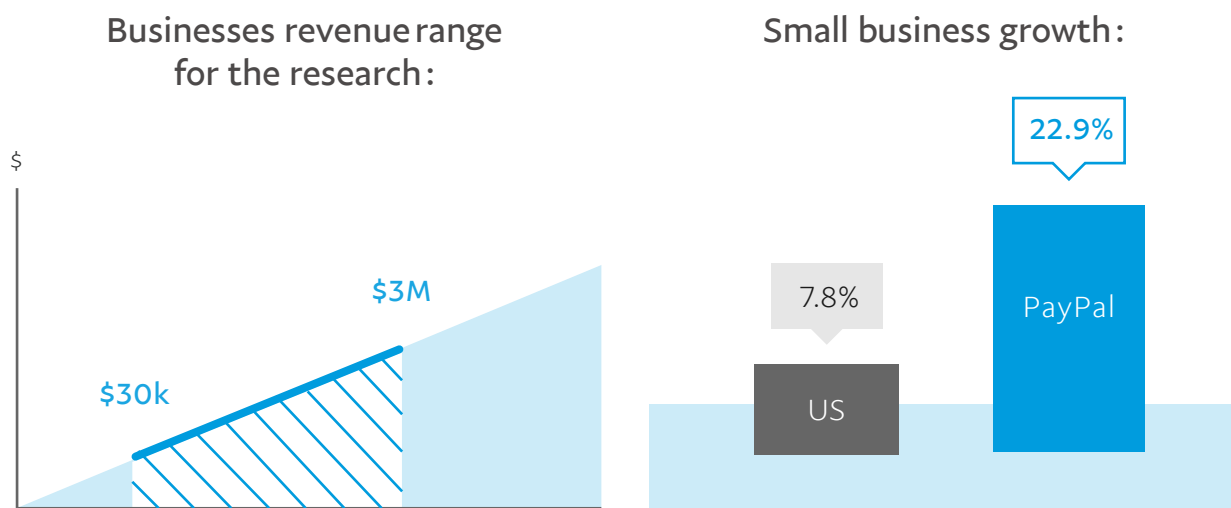
Businesses in nearly every sector can now engage in trade. A personal services firm located in suburban Missouri can now have suppliers in a small town in France and customers in over 30 markets. Moreover, small businesses no longer need to locate

in coastal areas or large cities to take advantage of globalization. The Internet provides equality of opportunity. A small business in Rexburg, Idaho and one in Manhattan, New York have access to the same 3.5 billion people using the Internet.

The remainder of this report will demonstrate how the Internet has transformed the outlook for small businesses and globalization through insights derived from studying a dataset of over 29,000 small businesses in the US using PayPal.

# Growth and Trade

There are about 28 million small businesses in the US, and they account for 52% of sales. US small businesses employed 56.8 million people or 48% of the private workforce in 2013. Small business under \$5 million saw 7.8% year-over-year revenue growth in 2015 according to accounting firm Sageworks; this was up from just 5% year-over-year growth in 2011.

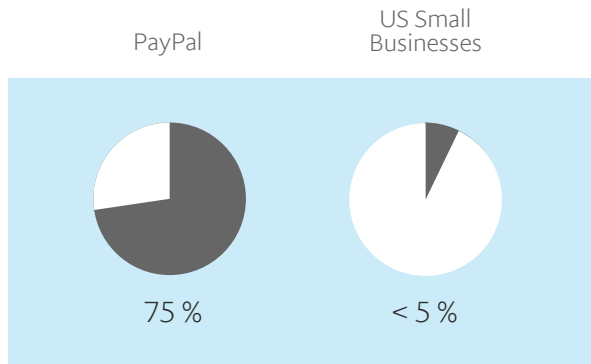


Our research on PayPal focused on businesses with annual revenue between \$30,000 and \$3 million. In the National Small Business Association's 2016 year end economic report over 65% of the small businesses were in this revenue range. These micro and small enterprises are the largest employers among small businesses; data from the census bureau shows that firms with fewer than 100 employees have the largest share of small business employment.

Small businesses using PayPal experienced growth patterns that are nearly triple the value of the typical small business. In the dataset we analyzed, small businesses using PayPal saw 22.9% year-over-year growth from 2015 to 2016.

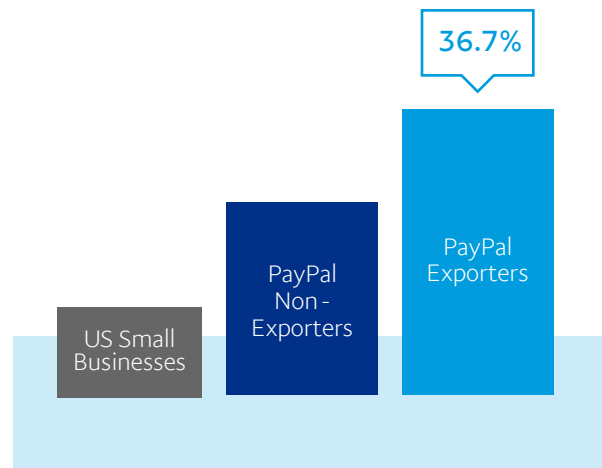


## Percentage of small businesses who export:



Less than 5% of small businesses in the US engage in exporting. There is a tremendous opportunity for small businesses to further embrace exporting. Businesses that use PayPal are disproportionately likely to be engaged in exporting; over 75% of small businesses in our sample data set engaged in exporting. This makes intuitive sense. The Internet is a borderless platform that enables instant connection with customers on the other side of the world. Marketing and marketplace platforms provide relationships and trust and financial services platforms enable cross border transactions to take place in different currencies efficiently and securely.

## Small business exporters using PayPal experience enhanced growth



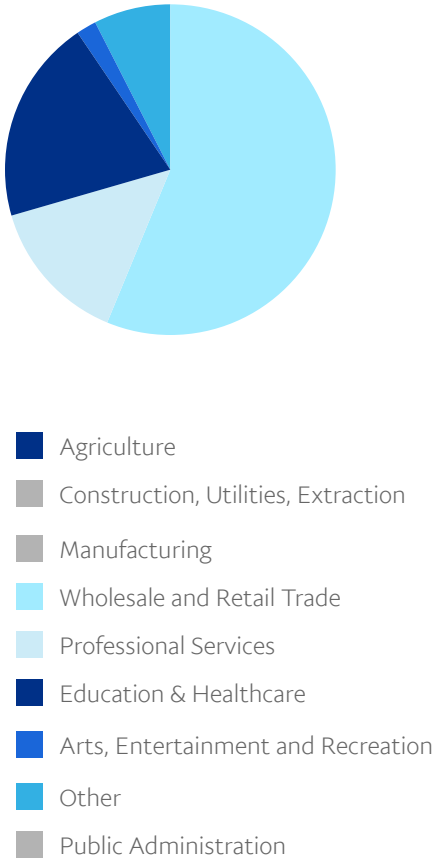
Exporting products and services yields enhanced productivity and employment. Literature on the gains from exporting have looked at total factor productivity (TFP) and found that exporters experience a premia of 4-18% in TFP. We found that exporters using PayPal experienced a revenue premia of 43% over non-exporters using PayPal, and a 421% premia over traditional small businesses. Small business exporters using PayPal grew 32.8% year-over-year from 2015 to 2016.

# Impacting Every Sector

Most research on exporting has looked at agriculture and manufacturing, in part because services were not often traded across borders. This was due to the fact that services typically required physical presence in order to be delivered across borders. Retail sales were done in person, administrative services required the employees to be in the same office, and technical services required onsite support. These were considered non-tradeable services. Research from eBay has demonstrated that retail is now no longer nontradeable.

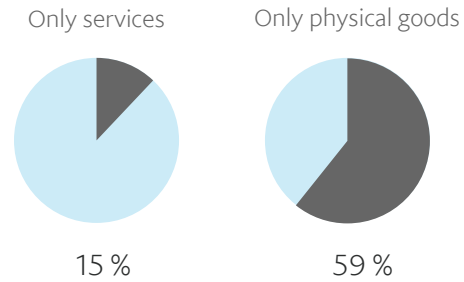
Our research now demonstrates that the impact of the Internet extends to nearly every subsector within services.

We excluded all eBay businesses from our sample set to eliminate the effect of the marketplace and to expand the data beyond retail trade. While a large number of the small business exporters that we looked at are in the retail sector, we also found a significant number of businesses in professional services, education, the arts, and other categories. This chart reflects who the businesses we looked at on PayPal can be subdivided by sector based upon the North American Industry Classification System (NAICS).



In comparison, a recent survey by the Export-Import Bank of exporting small businesses found that just 15% export only services. Most small businesses (59%) export only physical goods. Sean Luke, Vice President of Sales and Marketing at the Export-Import Bank stated that, *"this fits our understanding that many firms that deal in services struggle to find safe ways to export, while firms that export physical goods are often able to do so"*.

### What small businesses export:



#### Case Study:

## My Dreamlines

Nikki Gentry was a marketing professional who in 2014 decided to start her own business – My Dreamlines – providing custom gift portraits of wedding attire. About 15% of Nikki's revenues come from exports and one of her suppliers is located in France. Nikki's business of importing a picture from a customer, contracting with artists in foreign countries and exporting drawings are a type of personal services trade that would have been nearly impossible for a small business before the Internet.

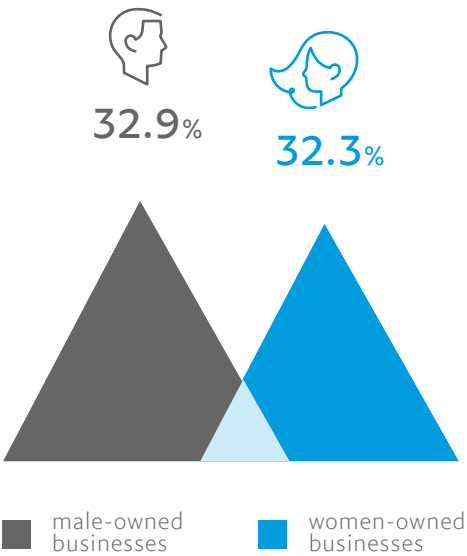
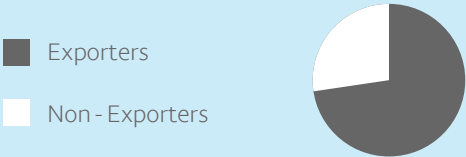
# Equality of Opportunity

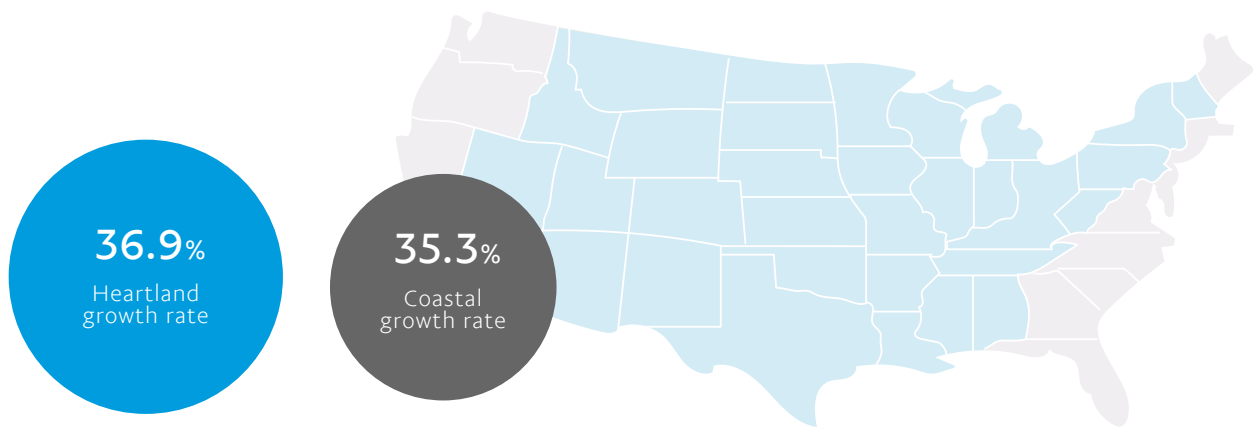
Women-owned businesses have traditionally seen a host of barriers to successfully starting and growing a small business. Women-owned businesses have also been less likely to engage in exporting than their male-owned counterparts.

The Internet enables women to grow and export on par with men. Nearly 3 of every 4 women owned businesses using PayPal that we studied export. Moreover, the growth rate for women-owned exporting businesses (32.2%) was nearly equivalent

to their male counterparts (32.9%). And, in certain parts of the country like North Dakota the percentage of businesses owned by women using PayPal is at parity with male-owned businesses.

## Women owned businesses (percentage of exporters):





Economies across the US did not grow equally in 2015; the most recent year for which data on state-by-state growth is available. Coastal states with large city centers like California, Florida, and Massachusetts grew above the national average. Whereas heartland states with large rural areas like Louisiana, Oklahoma, and North Dakota saw growth rates well below the national average and in some cases negative growth rates.

The Internet is enabling small businesses in the heartland and in rural areas to grow at unprecedented rates. Heartland small business exporters actually outperformed their coastal counterparts in 2016. In US towns with less than 50,000 people, small businesses using PayPal were just as likely to export and had similar growth rates the exporters had similar growth rates to their large city counterparts.

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*This recent data demonstrates a trend that has been occurring for some time, which is the clustering of growth and trade in a few city centers, generally located on the coasts.*

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# Policy Recommendations

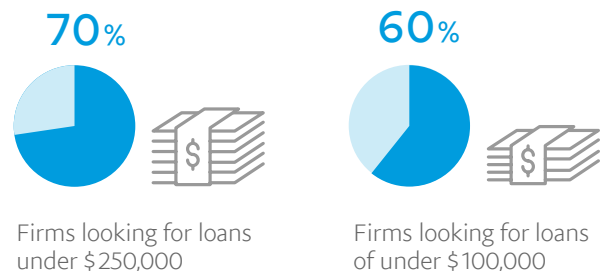
The analysis above demonstrates that small businesses can now reap the benefits of globalization due to the scale, trust, and access that is enabled through the Internet. There is still, however, a wide gap between what small businesses are doing today and their potential. The private sector is constantly innovating to provide small businesses with better products and services, but the public sector also has a role to play by creating an enabling environment for small business growth.

## 1. Access to Finance

Data from the Federal Reserve Bank of New York shows that managing cash flow is the top business challenge for 22% of firms and that the majority of small business owners hold some form of debt. Moreover, a decade of data from National Small Business Association (NSBA) surveys demonstrates a clear correlation between access to finance and a small businesses ability to hire more employees.

Smaller firms tend to be looking for smaller loans; over 70 percent of small businesses are looking for loans of under \$250,000 and more than 60 percent want loans of under \$100,000. US Federal Deposit Insurance Commission data demonstrates that commercial bank loans with principal less than or equal to \$1 million are down almost 14 percent from their 2008 peak. More than 30 percent of firms with under \$100,000 in revenues are turning to online sources for their credit needs. These loans

### Smaller firms tend to look for smaller loans:



are filling a gap by stepping in where other funding sources have pulled back. On-line issuance is projected to expand at a 47 percent CAGR through 2020, primarily through creation of new credit rather than taking share from incumbents. Moreover, these loans disproportionately serve businesses in places where retail banks have closed their doors, to lower-income businesses, and to younger firms.

Policymakers have a role to play in promot-

ing access to online small business financing tools. Government tools that point small businesses to traditional financing sources should now also point to online providers. Policymakers should seek to understand the variety of business models through which these loans are being provided and should avoid a one-size-fits-all approach. Lastly, policymakers should seek to understand what small business-

es need from a transparency perspective when looking at a short term cash flow loan; where total cost of capital may be the most relevant demonstration of how much a loan product costs.

## 2. Licensing

Nearly 20% of respondents to the National Federation for Independent Businesses' December 2016 Small Business Economic Trends report stated that government regulations and red tape were the single most important problem they face. Federal regulations affecting small business are often covered in the media, but international and state regulations can also disproportionately affect small businesses.

One of the most challenging regulations for small businesses seeking to expand beyond their locale are occupational licensing regimes. In the US, most states have occupational licensing regimes for careers in medicine, law, and increasingly several other types of fields. Moreover, countries around the world also have their own unique occupational licensing regime. Oftentimes these regimes are created with sound reasoning; one would not want a defense lawyer without the requisite knowledge of local evidentiary rules. Neverthe-

less, there are methods to ensure that a professional has the requisite knowledge of local rules without mandating a local license, and often local physical presence.

Passporting is the ideal policymaking tool in a world where services can be delivered across borders instantaneously.

If a professional has been granted a radiology license in Maryland, there is no reason that person should not be able to offer that service to a patient in Virginia, France, or Singapore. In order to create passporting regimes, however, policymakers must come together across state and country borders in order to certify that one another standards are interoperable. This is certainly no small challenge, but the benefits would be tremendous. If we want a world where the small service provider is truly global, we will have to come together to create passporting regimes for professional services.

### 3. Customs and Duties

When the digital world meets the physical world there can be frictions that inhibit cross border trade. A manufacturer, wholesaler, or retailer can now instantly market a product to customers around the world, but physically delivering those products remains a challenge. Antiquated customs and duties regimes disproportionately affect small businesses as they rarely have the resources to deal with divergent regimes. Moreover, the “importer” and many Internet-based cross border transactions are consumers; customs forms are often too complicated and parochial for an end consumer to understand.

Policymakers should be given credit for taking a major step in improving global customs and duties regimes through the signing of the World Trade Organiza-

tion Trade Facilitation Agreement in 2015. There is, however, more that can be done to facilitate small business cross border digital trade. Customs Application Programming Interfaces (APIs) would enable service suppliers to build customs and duties cost calculators and compliance forms directly into transaction flows, helping to reduce the burden on end consumers, small businesses, and governments. Governments should also require, or at least recommend, electronic submission and payment for customs and duties in order to speed up processing. Lastly, raising de minimis thresholds, the level below which customs and duties are exempted, should be raised and harmonized to facilitate trade done by the smallest businesses, which often deal in low value goods.

### 4. Digital Education

Over 40% of small business report to the National Small Business Association (NSBA) that economic uncertainty is the most significant challenge to future growth. The Internet can help to alleviate that concern by providing a global marketplace that can withstand local or even regional economic uncertainty. More than 25% of respondents to the NSBA survey report that they plan to expand their use of the Internet over the course of the next year; but, that means 75% are not looking into the value that the Internet might bring to their business. There is a significant need to educate small businesses on how they can take advantage of the Internet.

Many small firms are concerned that their product or service cannot be delivered across borders. Others are concerned about trust. Still others are concerned about getting paid. All of these problems have solutions, but it is a matter of making small businesses aware of these solutions. The Department of Commerce has an excellent program called Startup Global, which is designed to educate small businesses on how they can leverage technology tools to grow their business across borders. Local chambers of commerce, state governments, and municipal bodies should also incorporate the importance of technology tools into their small business educational materials.



For small firms that are online in some fashion there is still a great deal of digital education that must be done. These businesses need to learn about the wide variety of tools that can help them manage their business, secure it, and enable it to grow. A 2014 report from security firm Symnatec demonstrates that businesses with fewer than 250 employees are the victim of over 30% of cyberattacks. Even more problematic is the stat that 60% of small firms that are the victim of a cybercrime go out of business within six months of the attack. Policymakers again have a role to play in making small businesses aware of best in class security tools, as well as technology tools that can help businesses manage their finances and marketing.

Businesses with fewer than 250 employees are the victim of over 30% of cyberattacks.

Less than 20% of small businesses have IT staff. Governments can help to fill that void by providing small businesses with trusted guidance on how they can leverage the latest that technology has to offer to help their business grow.

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## Conclusion

The Internet does not discriminate based upon size, sector, gender, or location of a business. A woman-owned small business in a rural town can now leverage the Internet to grow and export. The Internet presents an unprecedented opportunity for inclusive growth. If we truly want to see a democratization of globalization, however, we are going to need concrete policy changes. Enhancing access to finance, creating passporting regulatory regimes, digitizing customs processes, and updating educational programs are going to be necessary steps on the path to making sure that every business is able to take advantage of the digital revolution. The public and private sector must work together on these solutions as the opportunity for inclusive growth is simply too great to pass up.

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