



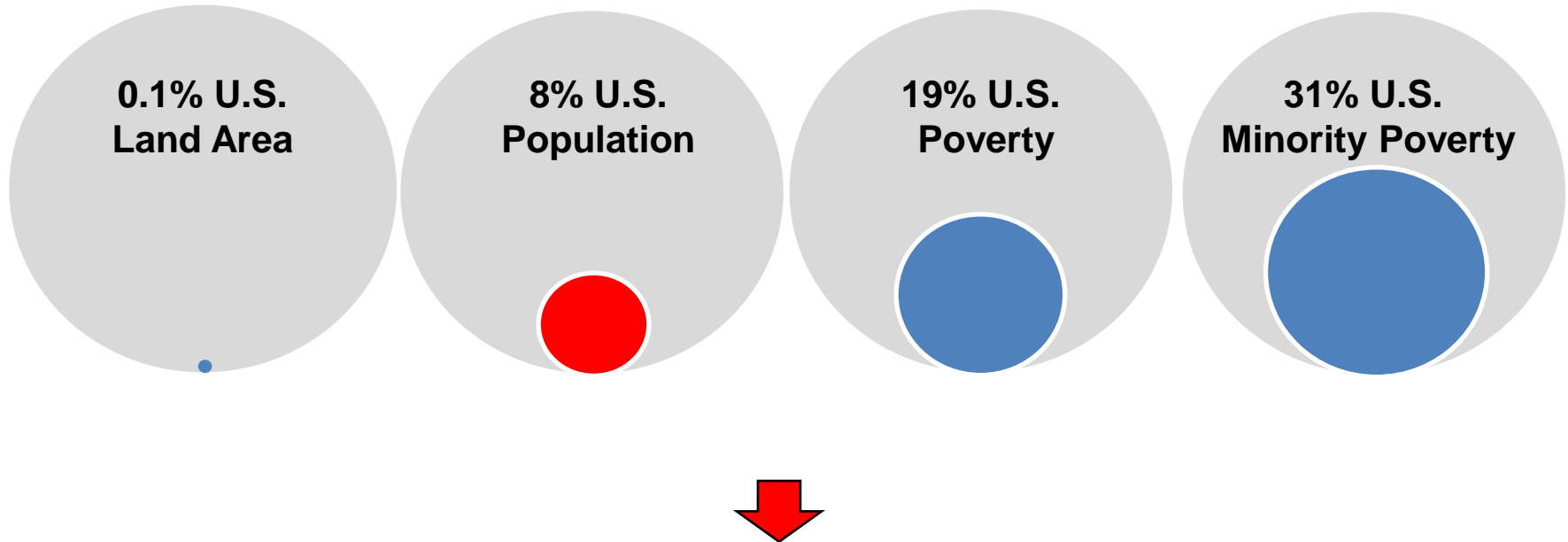
Initiative for a Competitive Inner City

Growing Successful Inner City Businesses: Findings From A Decade of ICIC Data

Dr. Michael Porter
Inner City Economic Forum Summit 2009
Washington DC
October 15, 2009

- Inner City Economies: Recent Performance
- Impact: Why Are Growing Firms in the Inner City Important?
- Characteristics of Growing Inner City Firms
- Factors Influencing Growth
- Implications for Firms and Policymakers

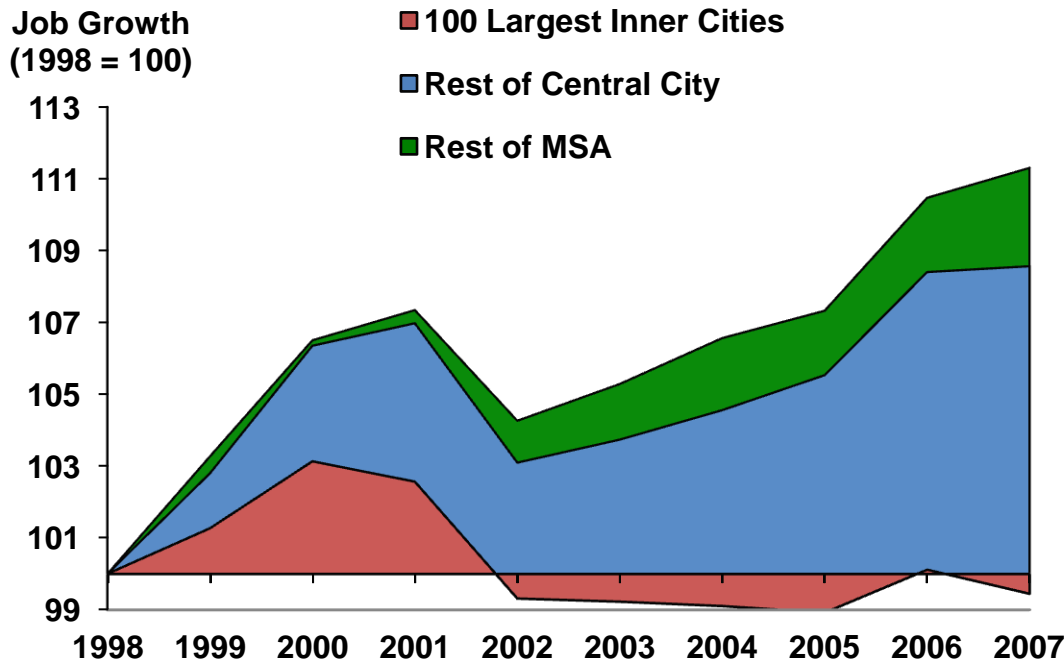
Poverty Concentration in the 100 Largest Inner Cities, 2000



- Targeting poverty in inner cities allows “**wholesale**” rather than “retail” approach to poverty reduction

- To identify inner city areas in the **100 largest central cities** and their associated ZIP Codes, ICIC follows a rigorous methodology
- ICIC's defines **inner city economies** as contiguous distressed neighborhoods of sufficient size to represent **meaningful economic sub-regions**
- Inner cities are defined as concentrations of **economic distress** in urban areas, measured by **poverty rates, income levels,** and **unemployment**
- Inner city poverty is quite **concentrated**. In 2000, the inner city areas accounted for the great majority of households living in poverty, with **sixty-five percent** of the poor in the 100 largest central cities living in inner city areas

100 Largest Inner Cities vs. Rest of MSA, 1998 – 2007



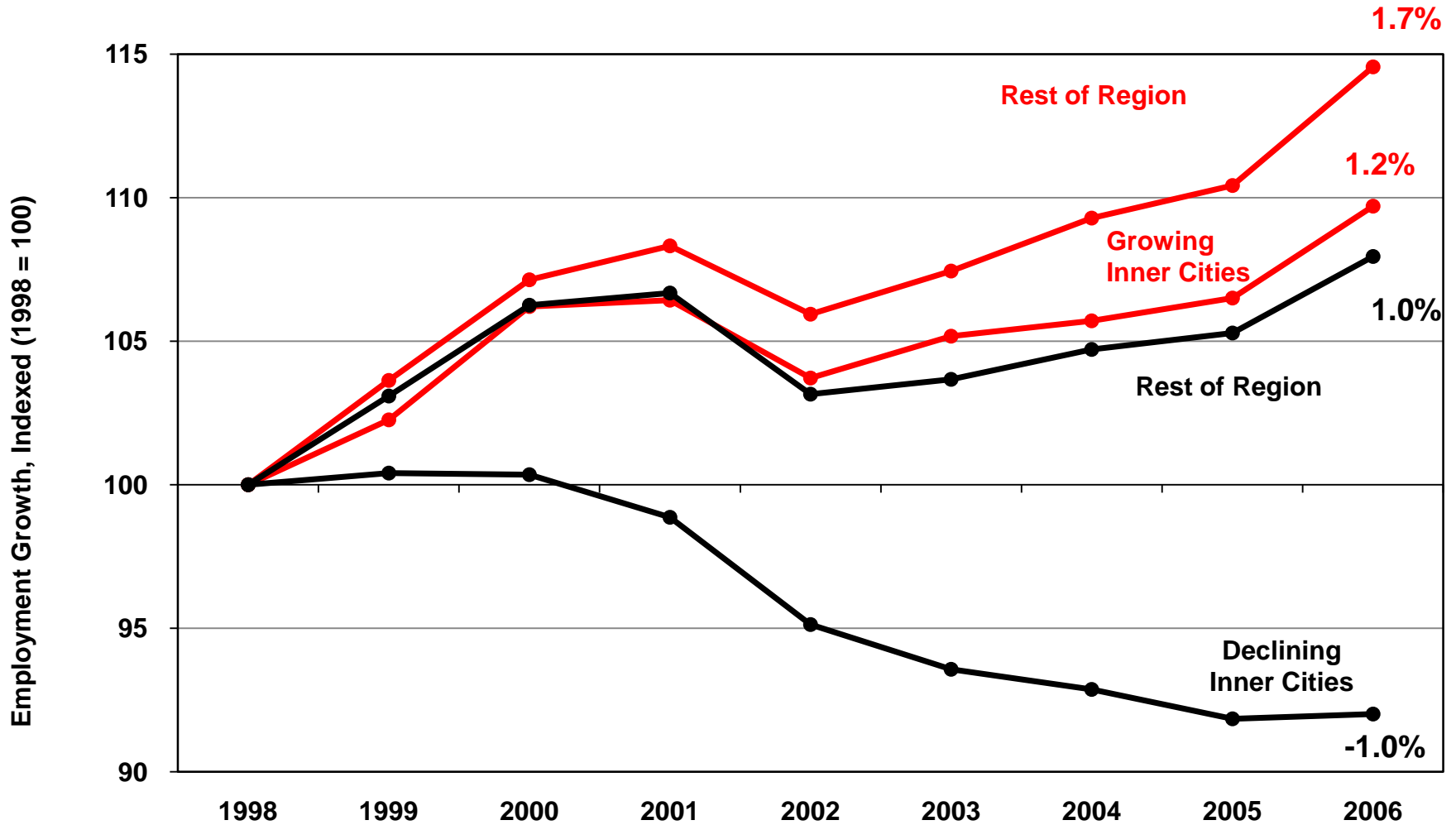
	1998 – 2007	
	Job Growth CAGR	Net Job Change
Rest of MSA	1.2%	+6,732,200
Rest of Central City	0.9%	+1,419,200
Inner City	-0.1%	-49,300



- Inner cities account for 8% of the U.S. workforce
- Between 1998 and 2007, the 100 largest inner cities were stagnant while their regions added over 6.7 million jobs

Inner City Job Growth vs. Rest of Region

Job Growth, 1998-2006

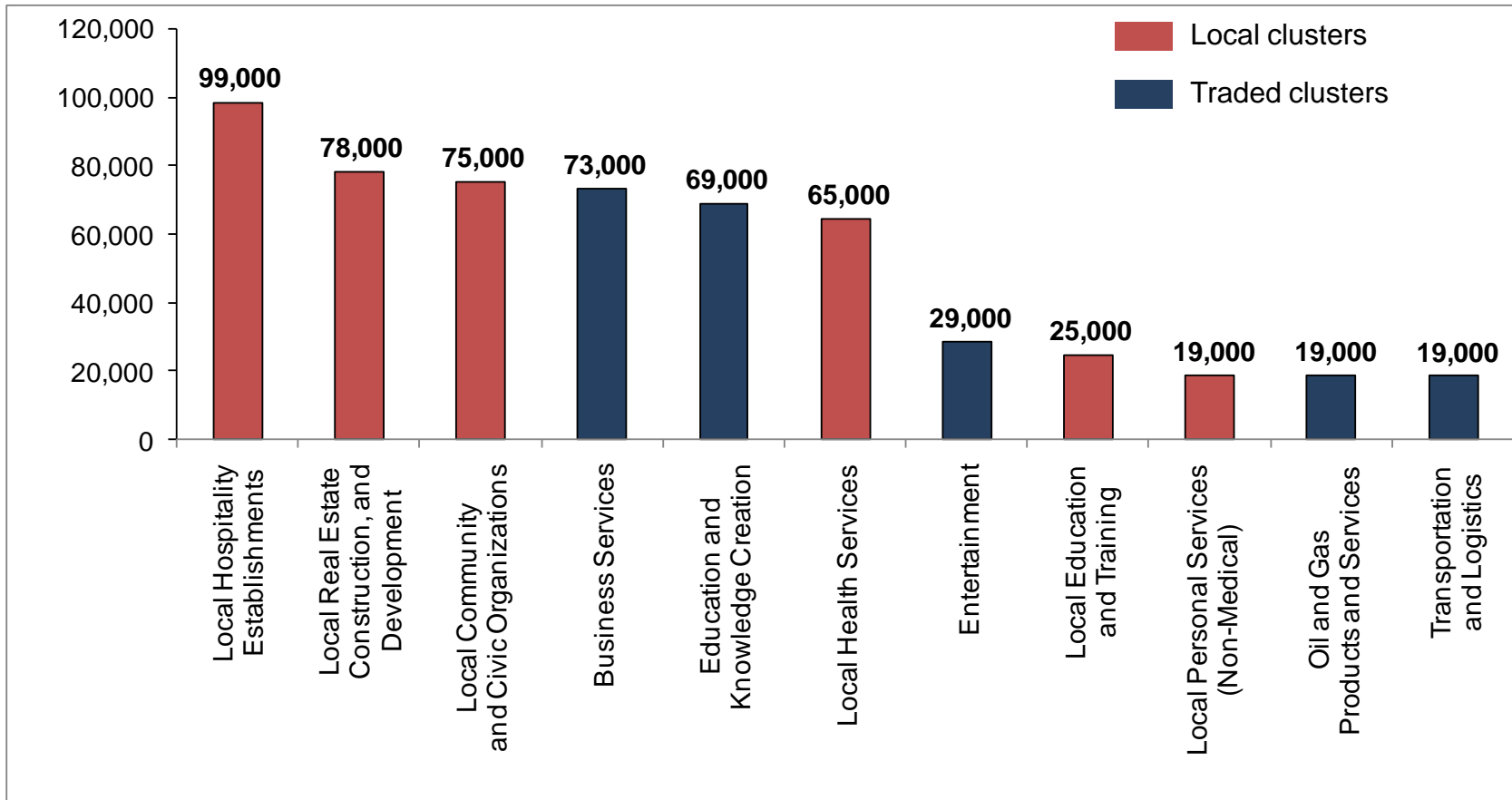


- Inner city decline has occurred even where there is regional growth

Factor	Evidence
Regional economic performance	Regional economic performance accounts for less than 10% of inner city performance
Globalization	Inner city economies are no more exposed to global competition than anywhere else in the U.S.; if anything they are less so
Technological advancement	Inner cities perform reasonably well in emerging sectors, including IT

- Outside factors account for a **small portion** of inner city performance

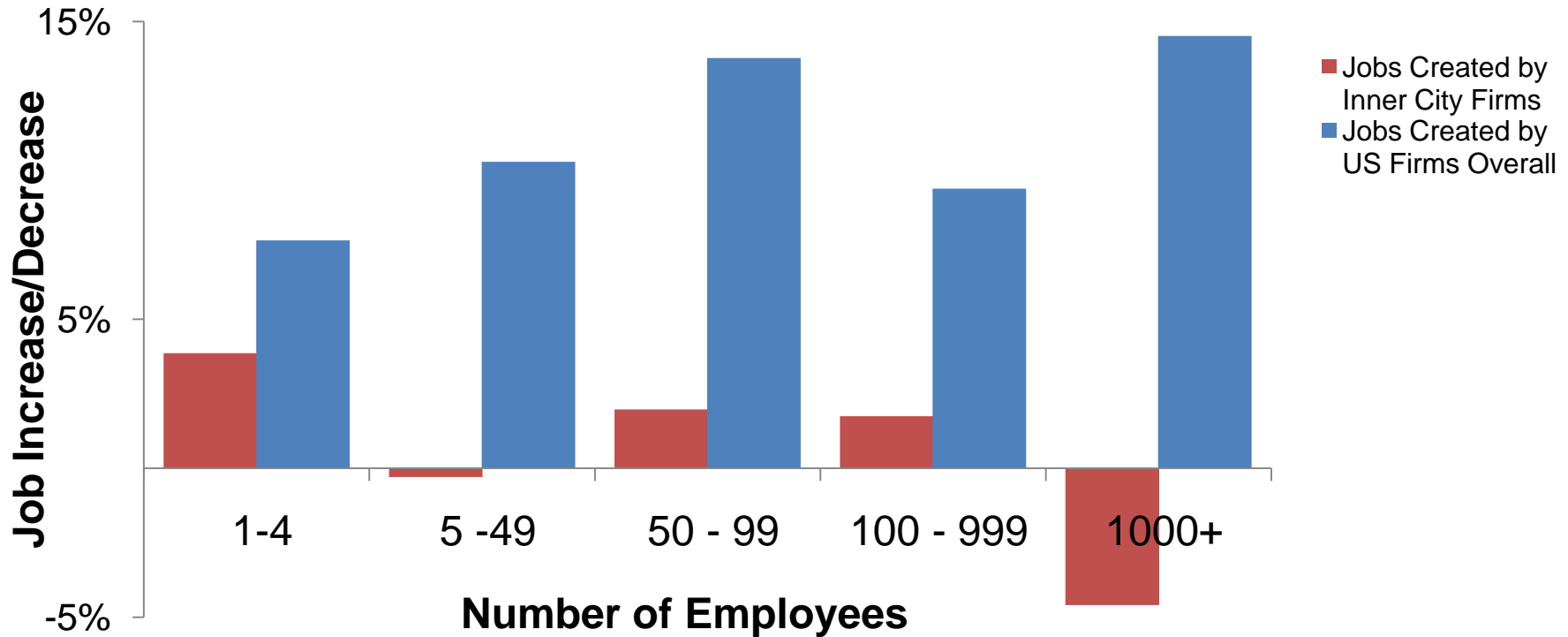
Inner City Job Growth, 1998 - 2007



- Inner cities have strengths in both **local** and **traded** clusters

Job Growth By Size of Firm

Inner City vs. US Overall (1998 – 2006)



- Large inner city firms have shown substantial job losses that more than offset gains by smaller firms

Inner City Business Environment

- Competitive advantage of Inner Cities
- State of inner city economies database
- Federal policy work

Inner City Clusters

- Retail cluster study
- University impact
- Small manufacturers
- Construction, housing & real estate
- Local cluster work

Inner City Firms

- Analysis of growing firms in inner cities
- Building proprietary database of inner city firms

Methodology

- ICIC has collected **firm-level data on almost 600 inner city firms** since 1999 through the **Inner City 100 program**
 - For-profit entities with a minimum 5-year operating history, at least \$1 million in revenue, at least 10 full-time employees and located in an inner city
 - Thriving companies that **leverage the competitive advantages** of doing business in inner cities
 - Unique and proprietary data that helps us understand the factors that **enable inner city firms to succeed** and the **obstacles** they face
- For the first time, we have been able to **benchmark** data on **successful inner city firms** against data on all **inner city firms**, all **U.S. firms** and **comparable firms** outside the inner city
 - Kauffman Firm Survey (KFS) database of 5,000 US Firms started in 2004 with 3 years of longitudinal data

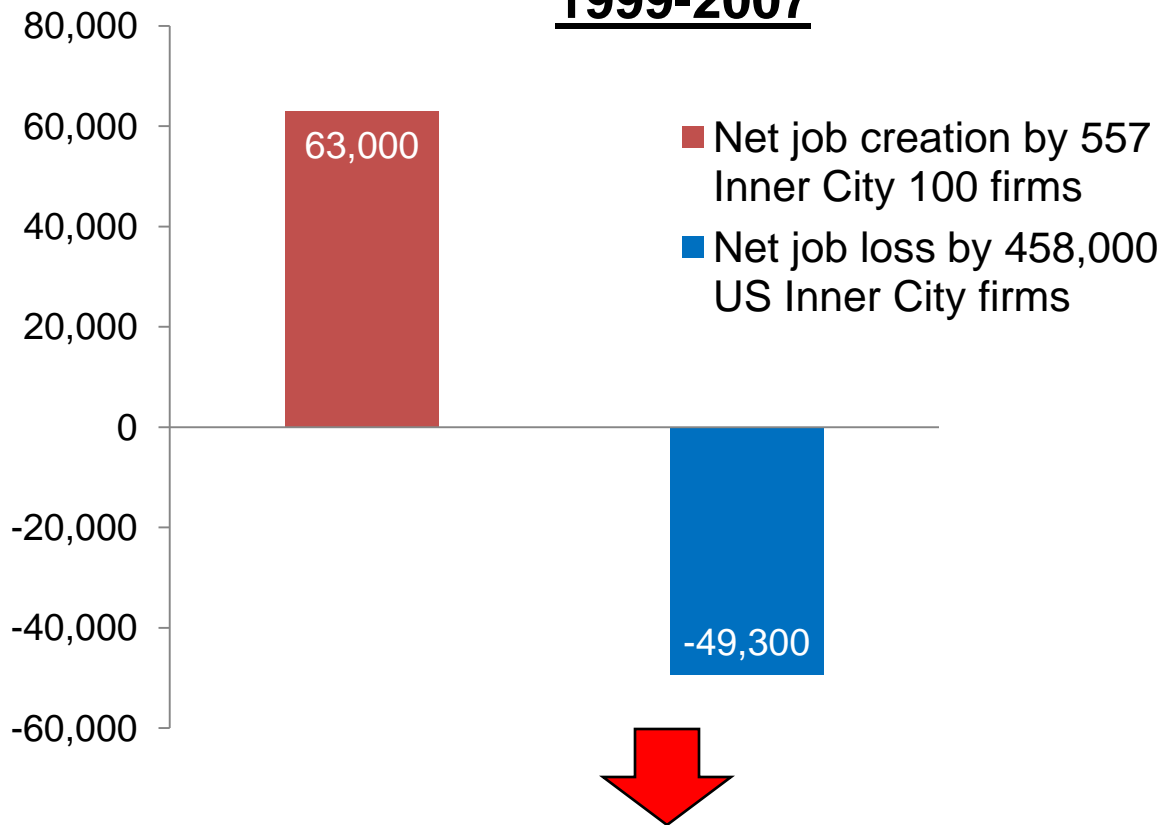


- The goal is to inform **company strategies** and **stakeholder actions**

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- **Impact: Why Are Growing Firms in the Inner City Important?**
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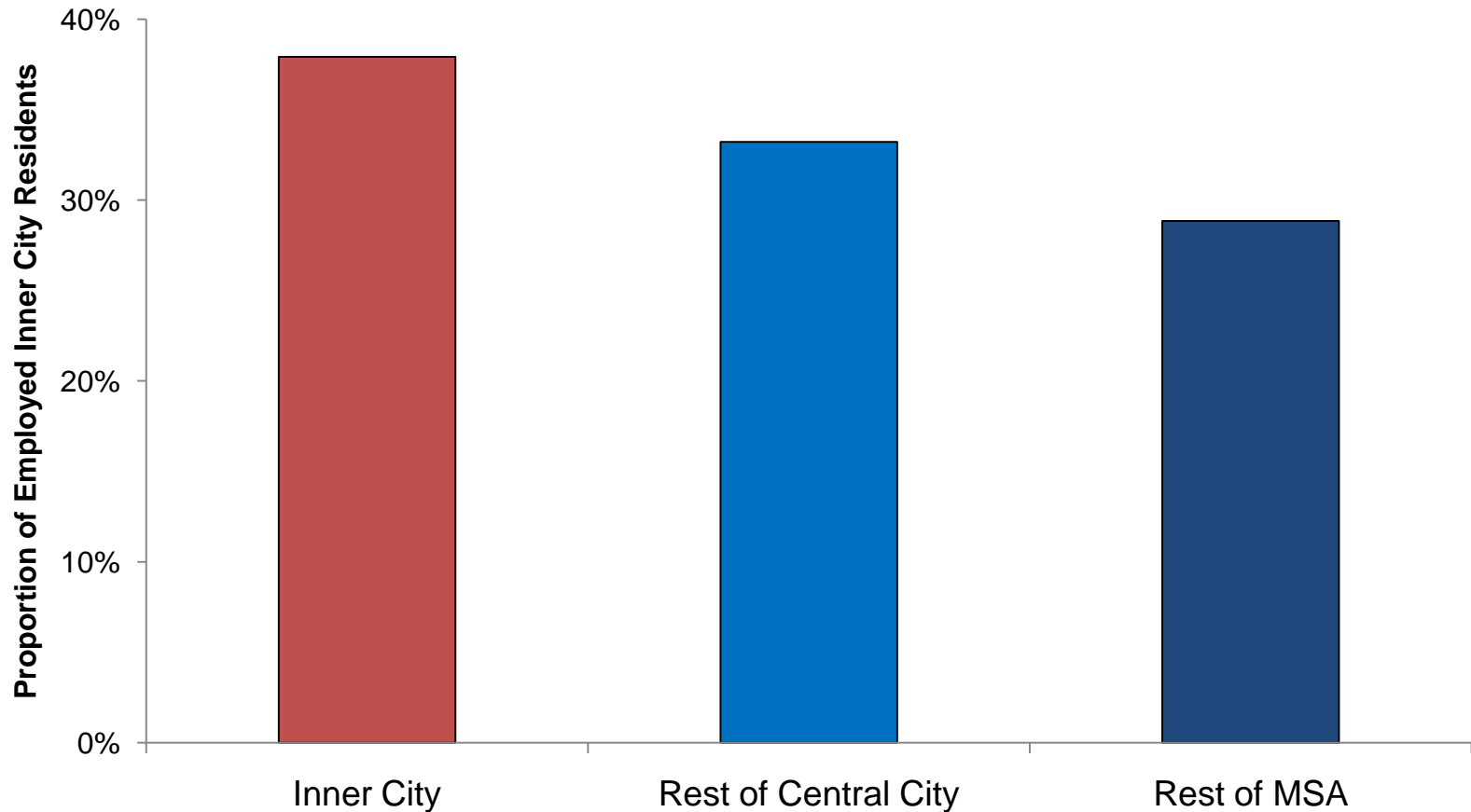
The Impact of Inner City 100 Firms on Inner City Economies

Inner City 100 Job Growth vs. Total Inner City Job Growth, 1999-2007



- A small number of rapidly growing firms can have a tremendous impact on inner city job creation and economic revitalization

Inner City Residents' Job Location Distribution, 2000



- Residents of the inner city more frequently **work in the inner city**



ICIC Location of Job Creation and Inner City Resident Employment

In a typical U.S. region inner city residents hold:

- 22% of the jobs in the inner city
- 11% of the jobs in rest of the central city
- 7% of the jobs in the rest of the region

Creating 100 new jobs for inner city residents would require:

- 450 jobs in the inner city
- 850 jobs in the rest of the central city
- 1,450 jobs in the rest of the region



- “Jobs anywhere” are **not enough**. Often inner city residents have difficulty accessing jobs in the rest of the region

Community Involvement

Interviews with Inner City 100 Firms

Volunteer Work

- Hope House
- Multiple Sclerosis Society
- Paraplegic Veterans Association
- Green for All
- Community Gate Path
- United Way
- Allie's House
- Special Olympics

Philanthropic Investments

- Creating scholarships and intern programs at inner city schools
- Sponsoring needy families
- Donations to a local historical theater
- Financial incentives to employees using public transportation
- Donations to charter schools

“Charities are a large part of the corporate culture, and many employees value the opportunity to give back to the community through their jobs.”

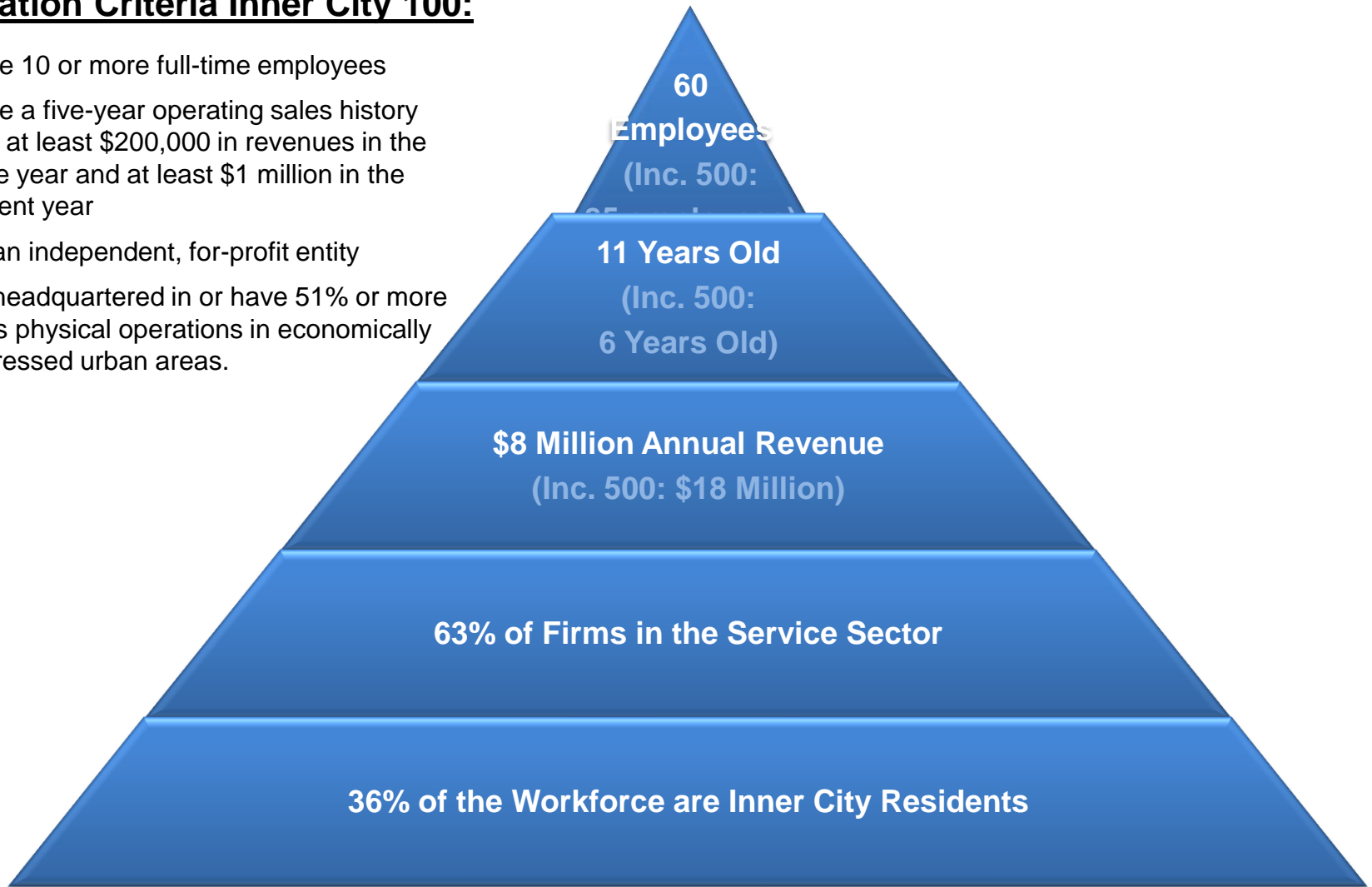
- *CEO of a Technology Company, 2009 ICIC Interview*

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Snapshot of a Typical Inner City 100 Firm

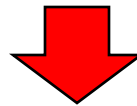
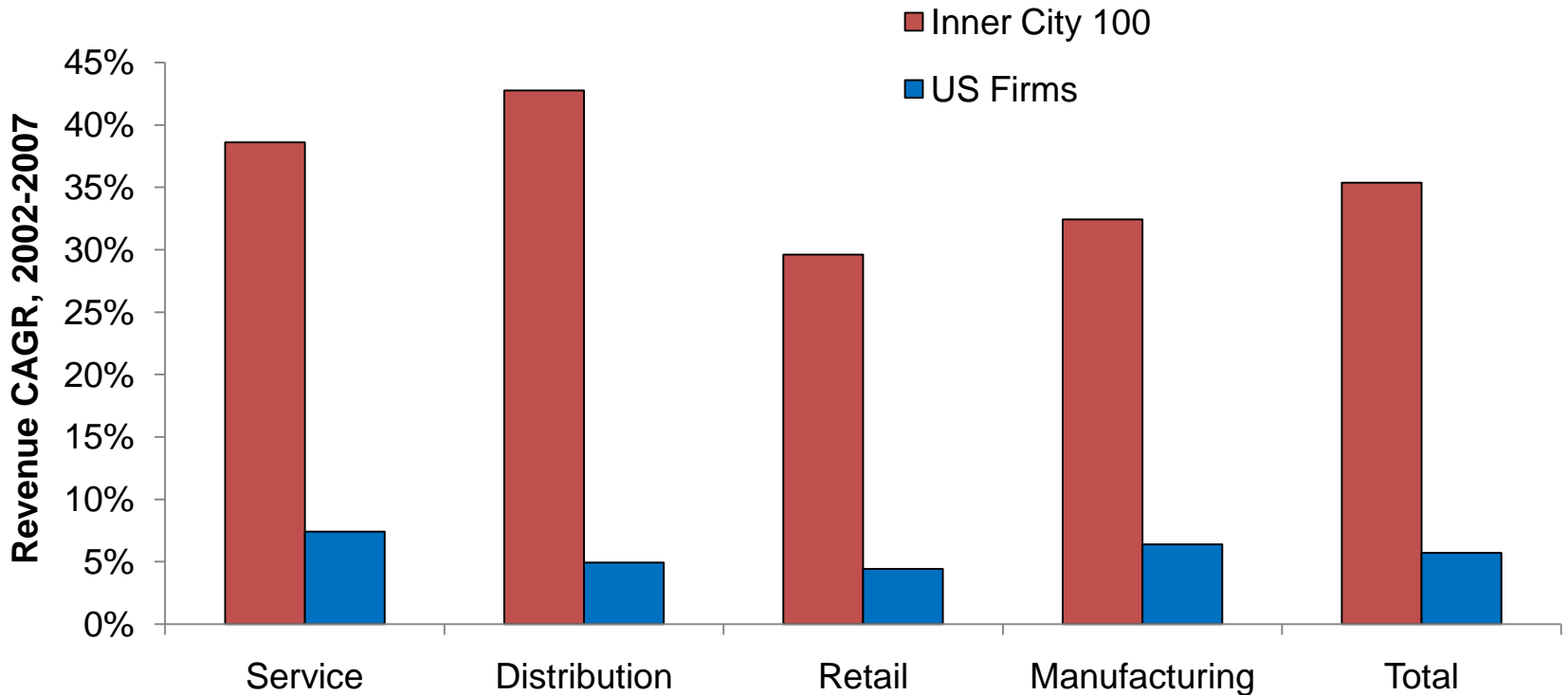
Application Criteria Inner City 100:

- 1) Have 10 or more full-time employees
- 2) Have a five-year operating sales history with at least \$200,000 in revenues in the base year and at least \$1 million in the current year
- 3) Be an independent, for-profit entity
- 4) Be headquartered in or have 51% or more of its physical operations in economically distressed urban areas.



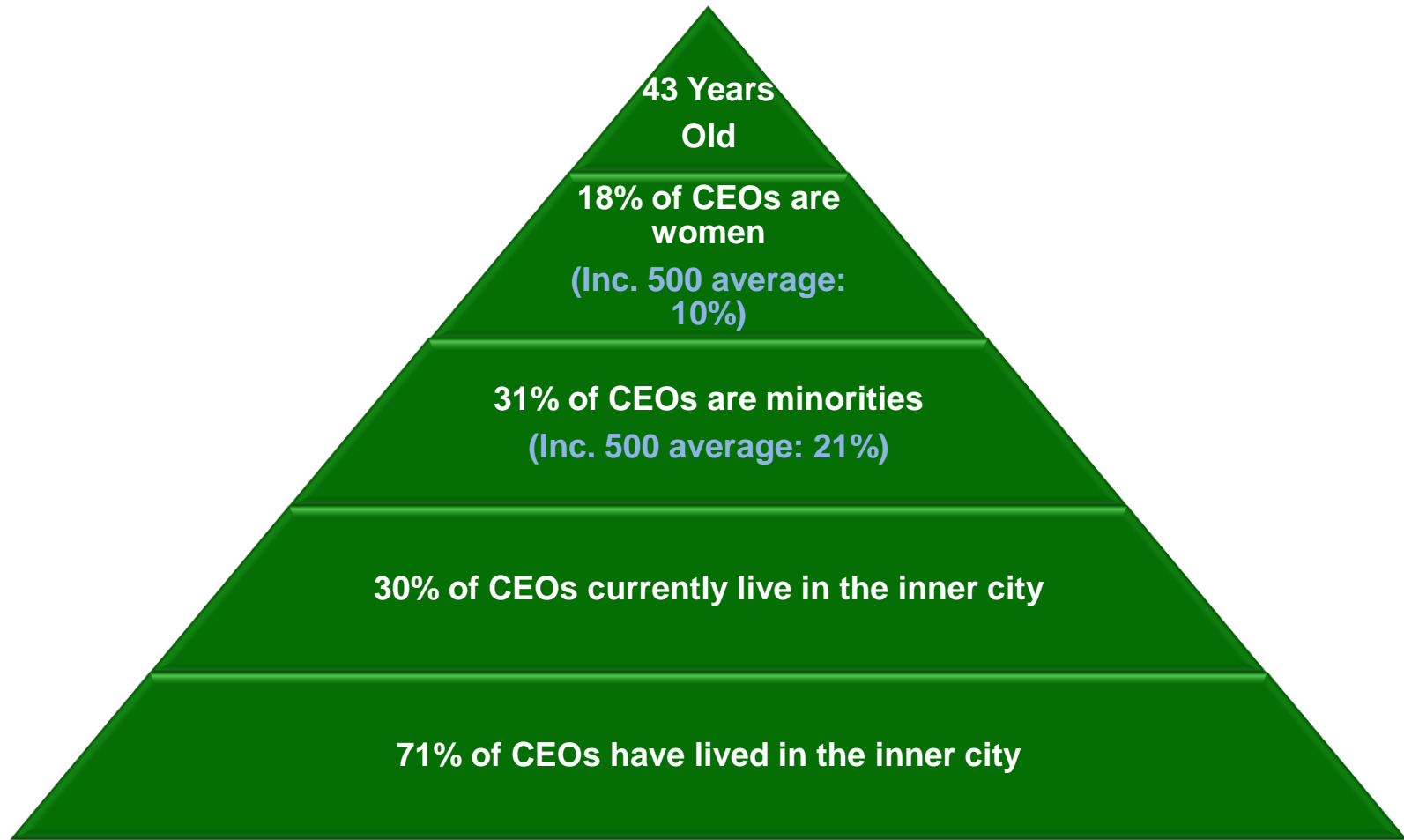
Inner City 100 Firms

Revenue Growth vs. Sector Averages



- Inner City 100 firms have much higher revenue growth across **all sectors**

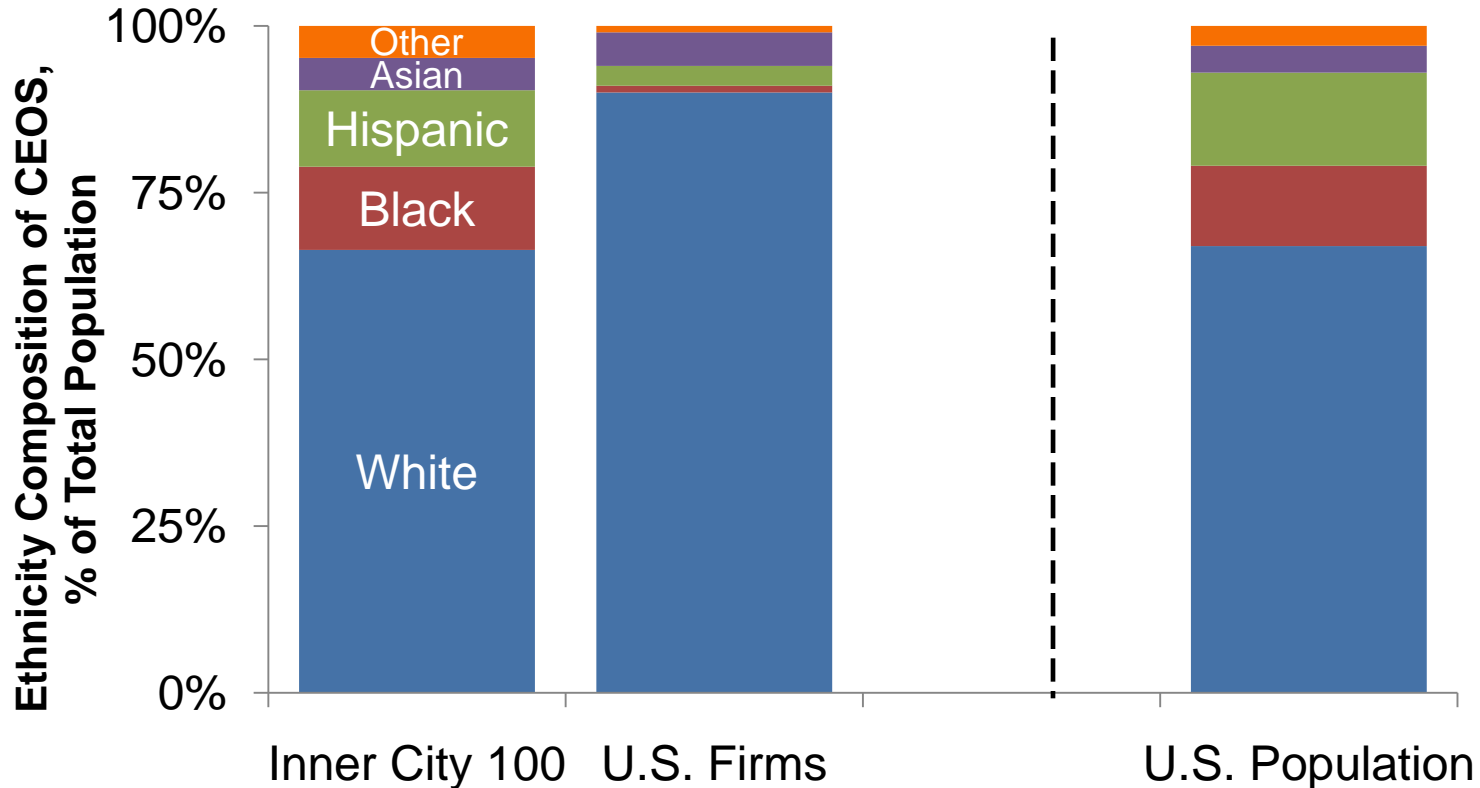
Snapshot of a Typical Inner City 100 CEO





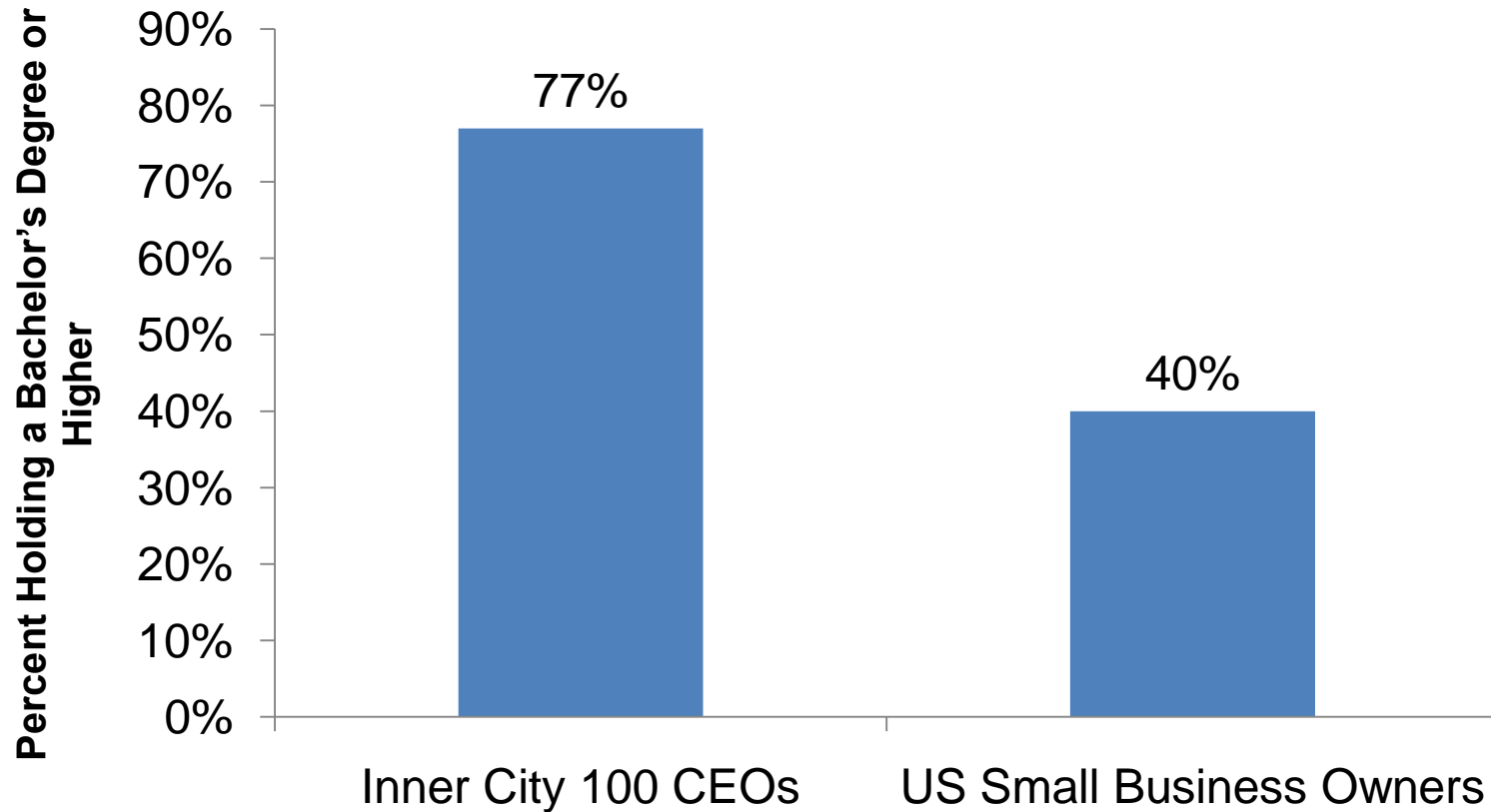
Inner City 100 CEO Demographics

Ethnicity of Inner City 100 CEOs vs. US Firms and US Population



- Inner City 100 CEOs are more ethnically diverse than CEOs of US firms overall and mirror the demographics in the overall US population

Inner City 100: Proportion of CEOs and Business Owners with Advanced Degrees



- Inner City CEOs are **more educated** than US small business owners overall

- Inner City Economies: Recent Performance
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ICIC Factors Influencing the Growth of Inner City Firms

Financing

- Access to Capital
- Sources of Capital

Inner City Business Environment

- Advantages
- Disadvantages
- Use of Public Programs

Company Revenue Sources

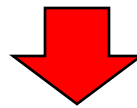
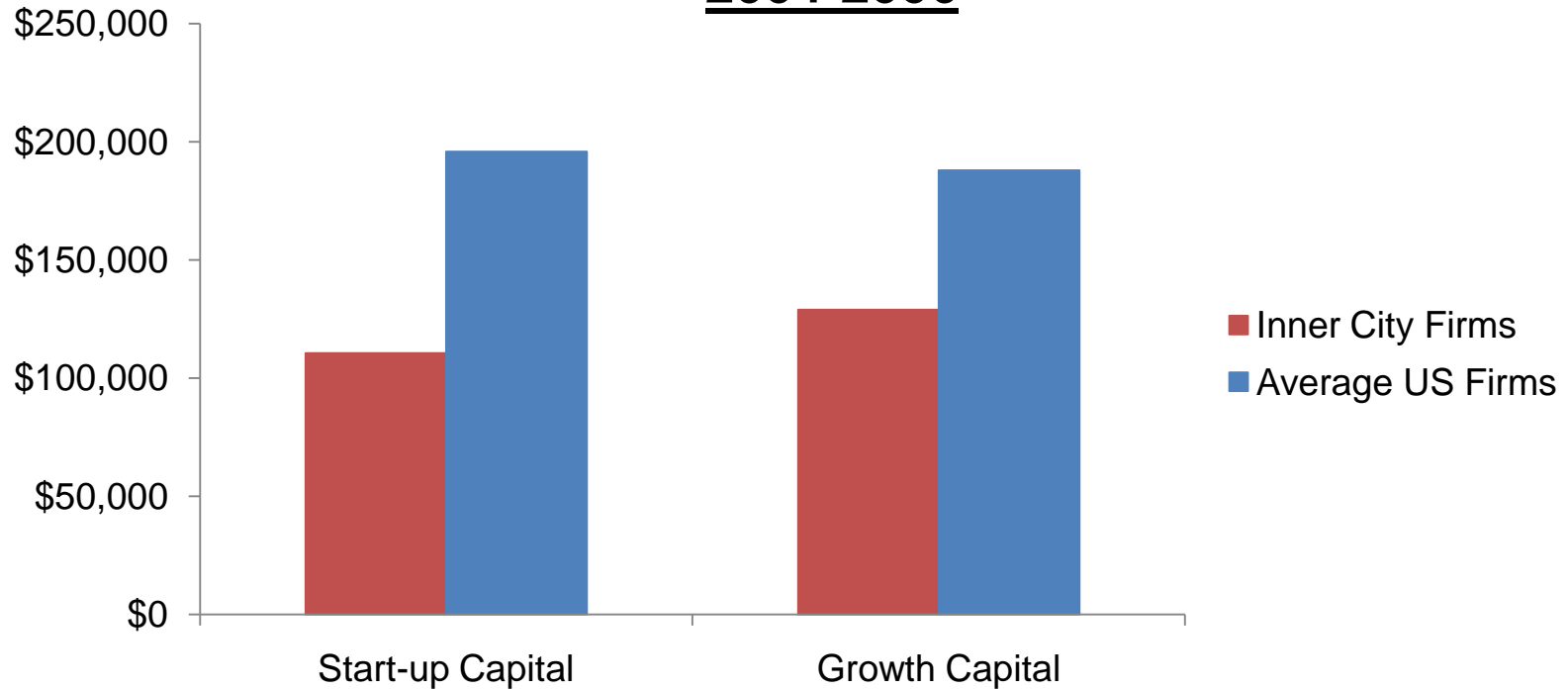
- Customer Composition
- Government Contracts

Leadership and Human Capital

- CEO Background
- Inner City Workforce
- Employee Benefits and Training

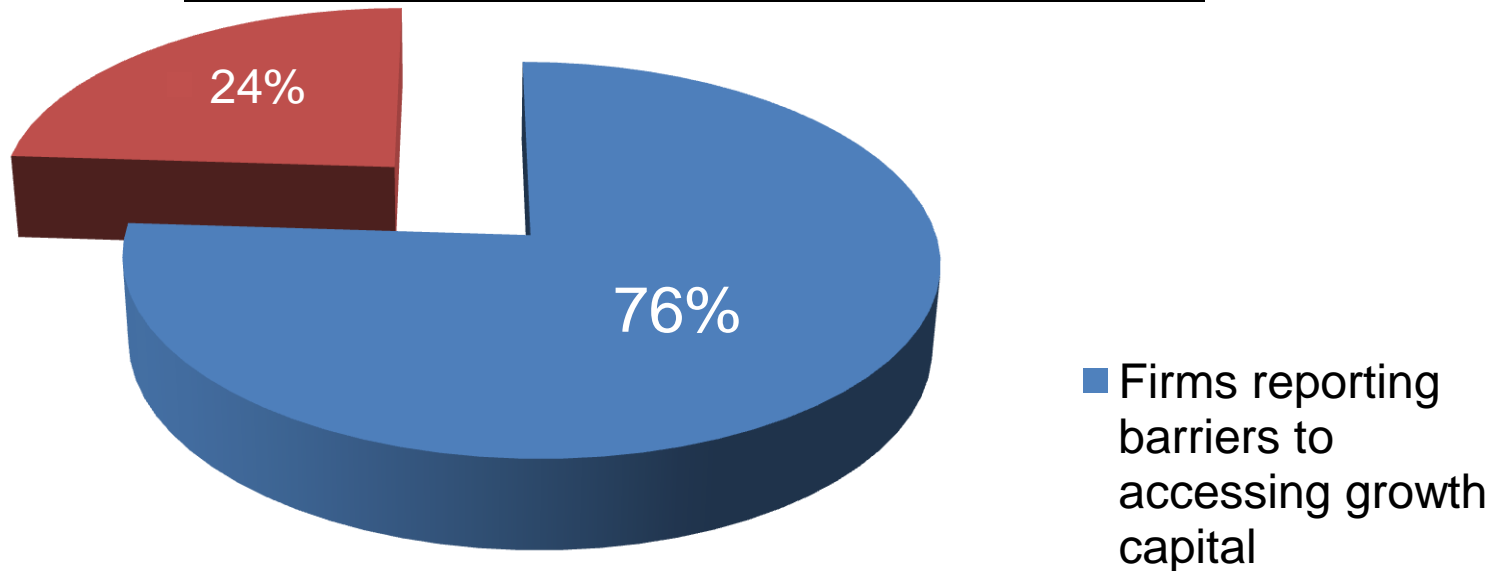


Start-up and Growth Capital for Inner City Firms vs. All US Firms, 2004-2006



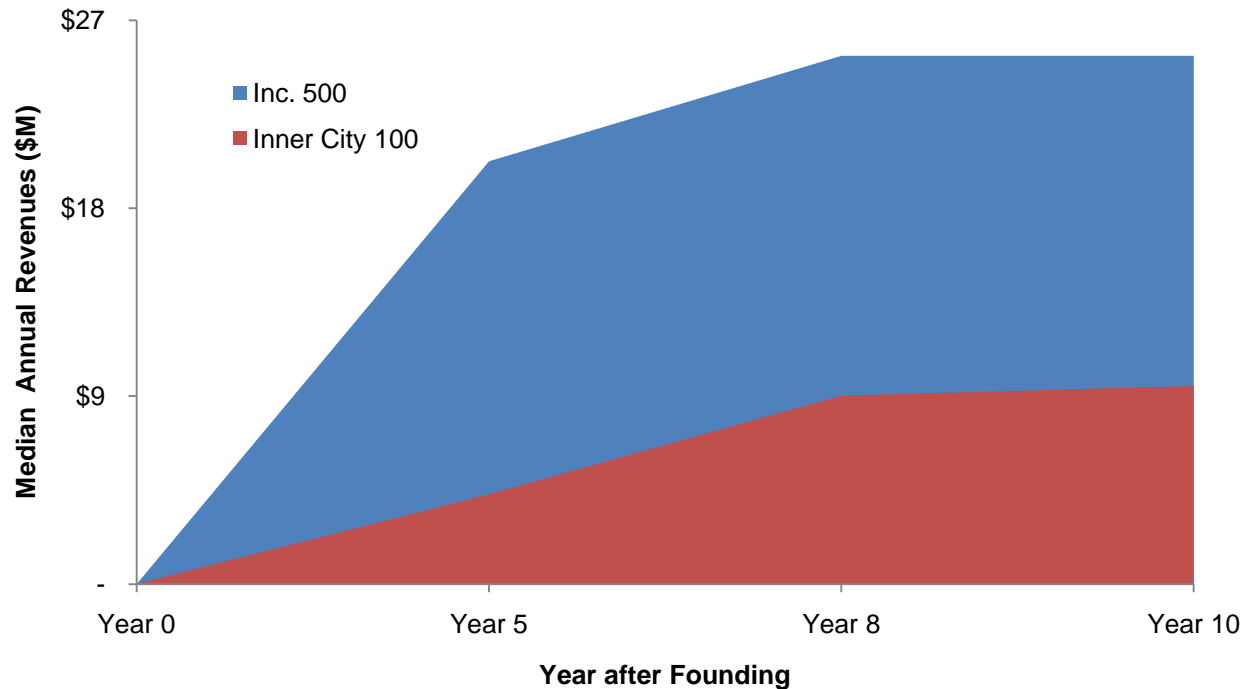
- Inner city firms utilize **44% less startup capital** than average US firms and **31% less growth capital**

Inner City Firms Reporting Barriers to Accessing Growth Capital, 2008-2009



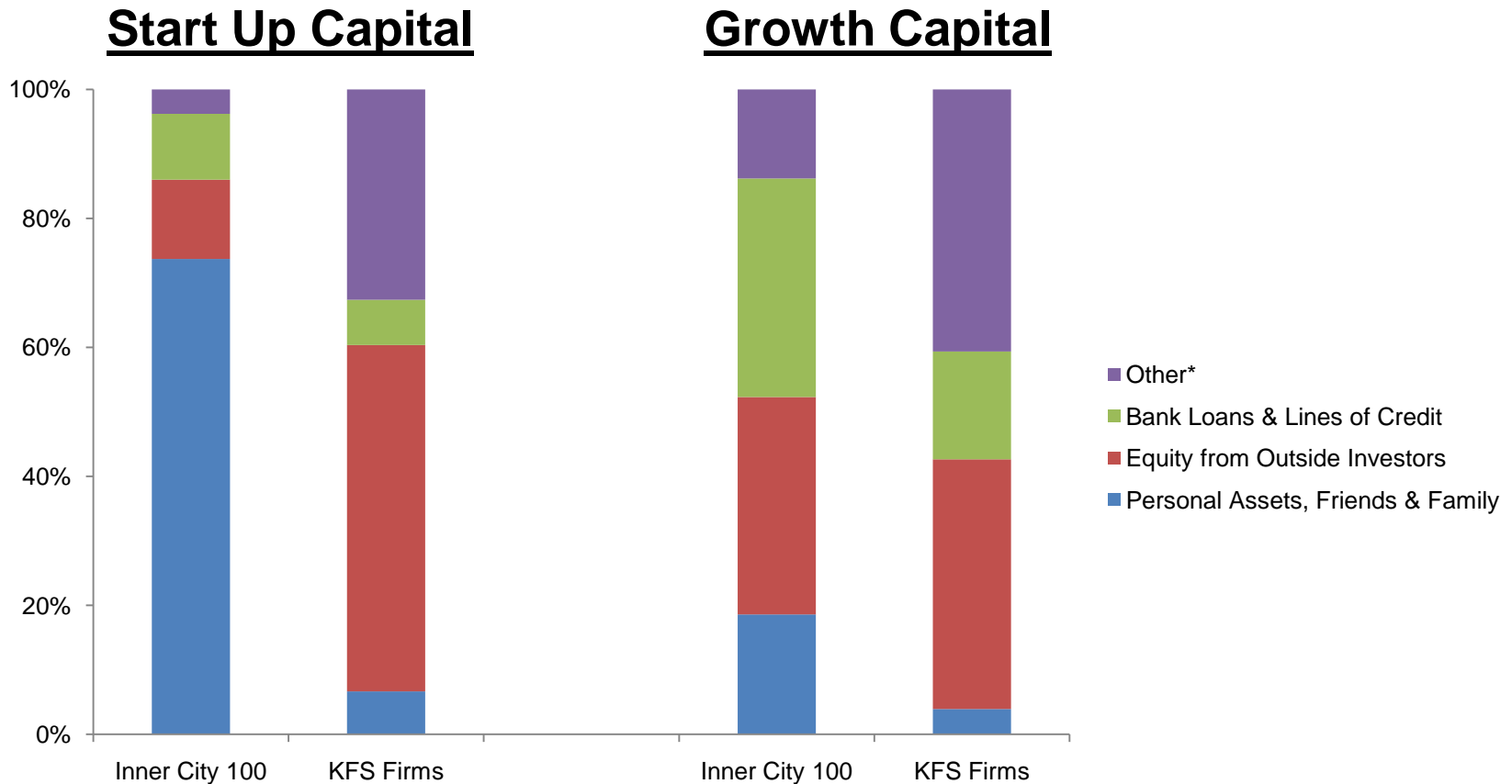
- 
- 76% of growing inner city firms reported experiencing barriers to accessing growth capital

Revenue Growth of Inner City 100 firms versus Inc 500 Firms, Year 0 – Year 10 of Firm Lifecycle



- Limited capital seems to influence growing inner city firms' **ability to accelerate growth** and reach the same **scale** as growing non-inner city firms
- Inner city firm CEOs frequently run business for **cash flow rather than growth**

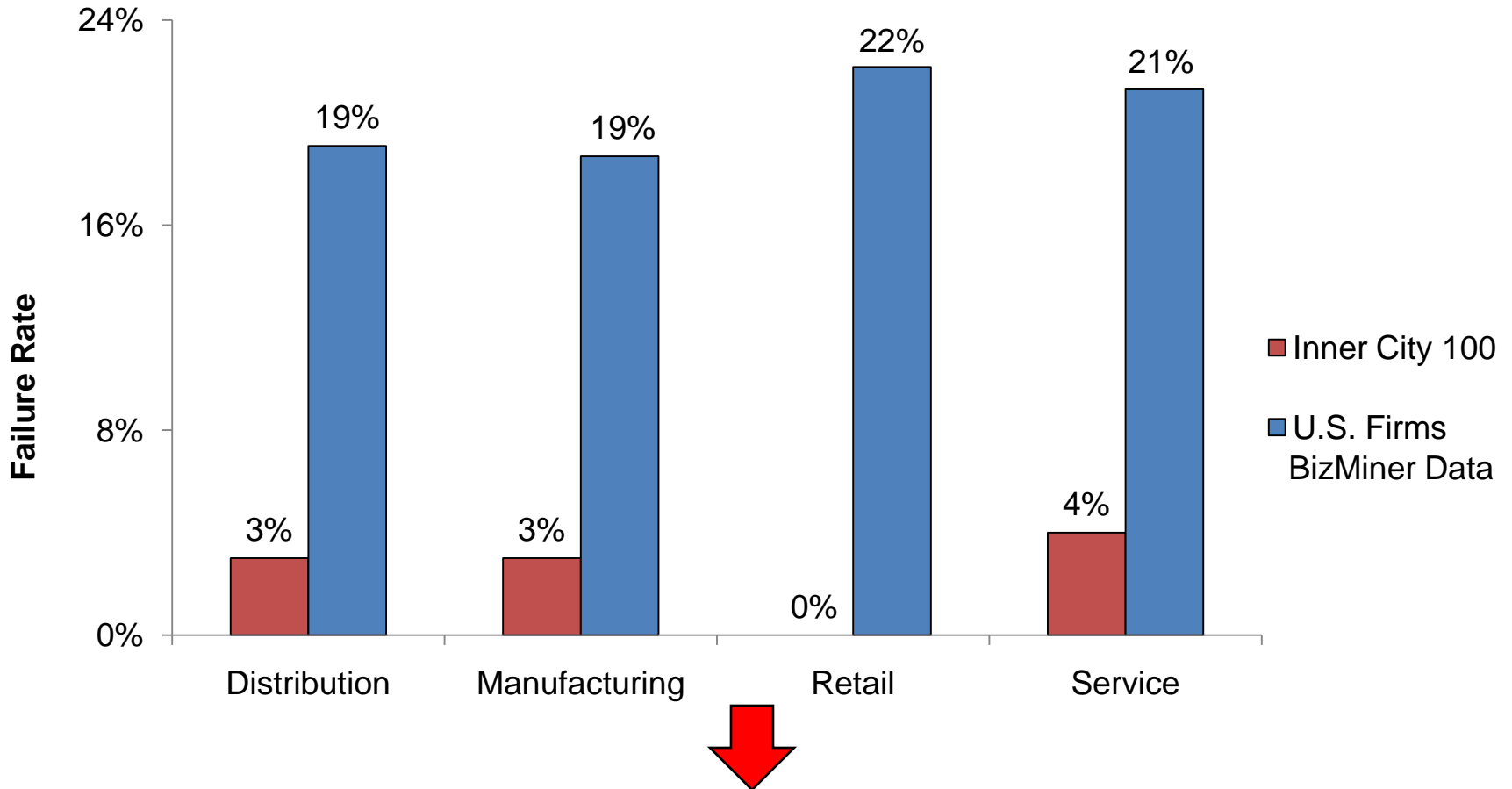
Financing: Sources of Start-up & Growth Capital, 2004-2006



- Inner City 100 firms tend to be **more conservatively capitalized**, relying more heavily on personal assets for start up and more bank loans to grow

Financing: Low Failure Rates

Failure Rates by Sector, Inner City 100 vs. US Firms



- Over the past 11 years, only 16 Inner City 100 firms have gone out of business, none within the retail sector

“Capital access is a vicious cycle; without money, it is almost impossible to get money. We took out a \$50K line of credit with a bank, but we use this as more of a convenience, rarely relying on the debt and paying the balance off immediately so as not to accrue interest charges.”

- *Chief Strategy Officer, Advertising & Marketing Firm, 2009 ICIC Interview*

- Limited access to capital affects inner city firms' growth trajectories
- Heavier reliance on debt and internally generated funds means many inner city firms prioritize cash flow over growth
- Lower amounts of start-up capital drive inner city firms into less-capital intensive industries
- Because Inner City 100 firms are more conservatively capitalized, they tend to have lower failure rates than the national corporate average



ICIC Factors Influencing the Growth of Inner City Firms

Financing

- Access to Capital
- Sources of Capital

Inner City Business Environment

- Advantages
- Disadvantages
- Use of Public Programs

Company Revenue Sources

- Customer Composition
- Government Contracts

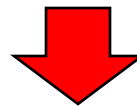
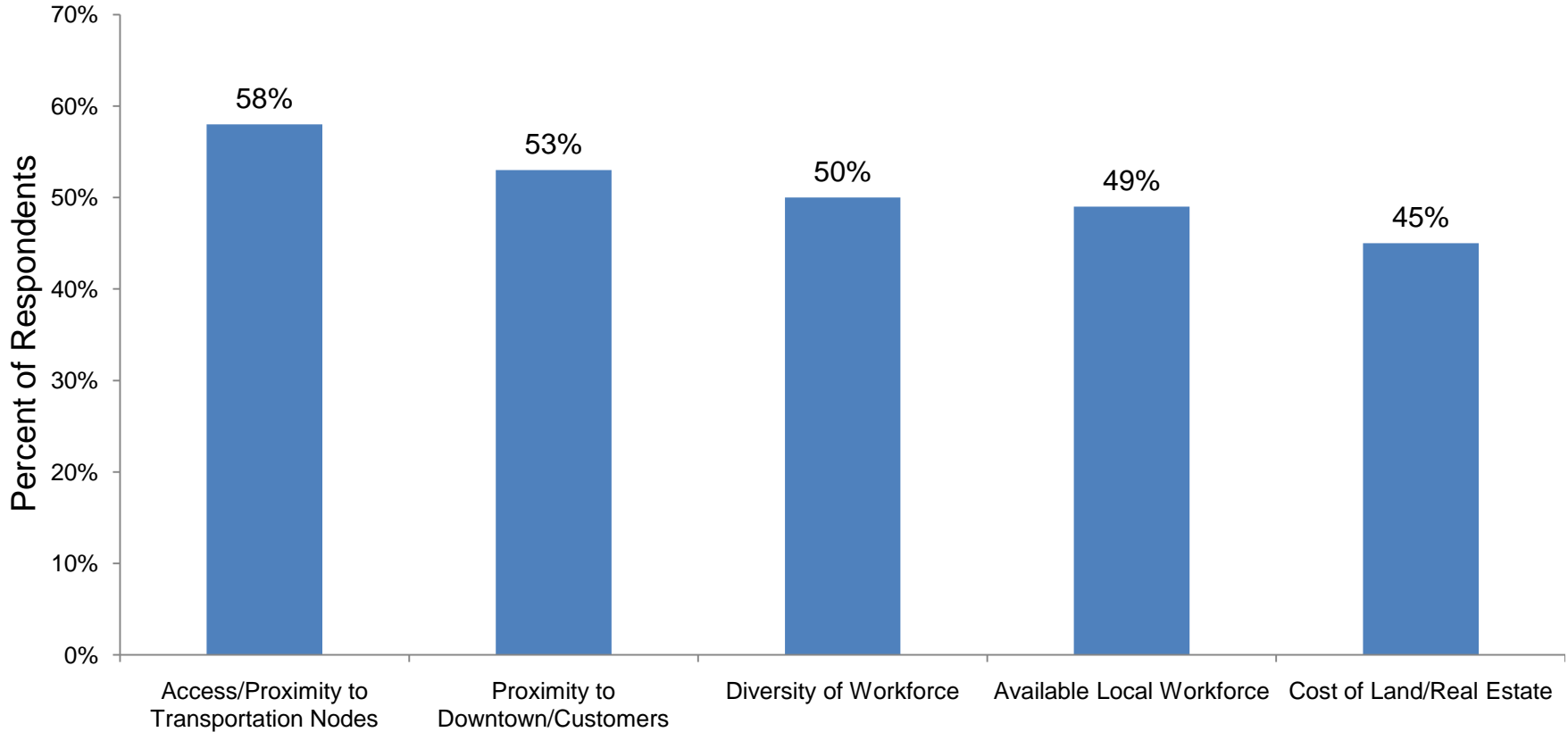
Leadership and Human Capital

- CEO Background
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ICIC Business Environment: Advantages of Inner City

Most Cited/Highest Ranked Advantages, 2004-2009

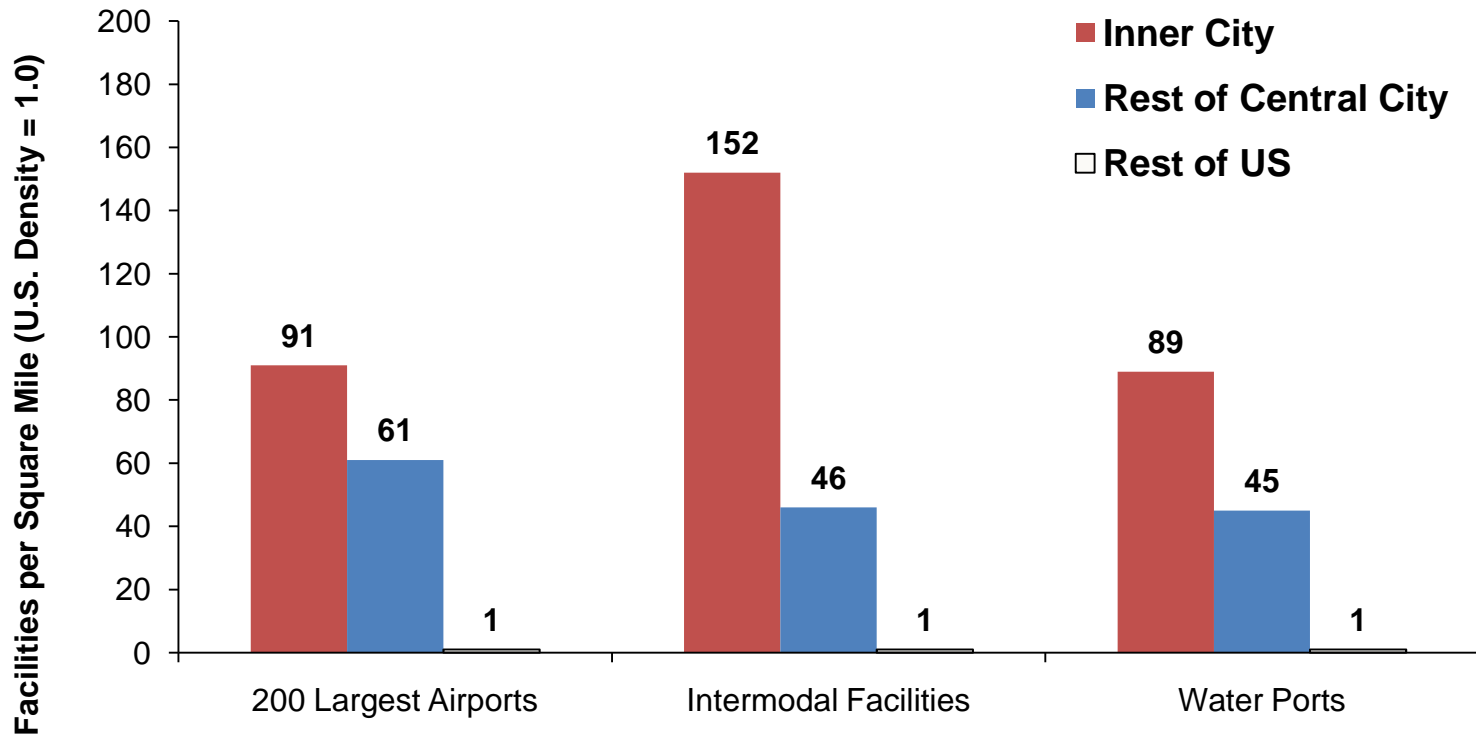


- Access and transportation are cited by Inner City 100 firms most frequently as advantages of their location

Source and Notes: ICIC analysis of Inner City 100 Survey data, 2004-2009, n=504. Respondents chose up to 3 factors out of a list of 10. (2004-2006) or ranked 1 or 2 on scale of 1 to 7 (2008-2009).

Business Environment: Location of Transportation Assets

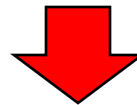
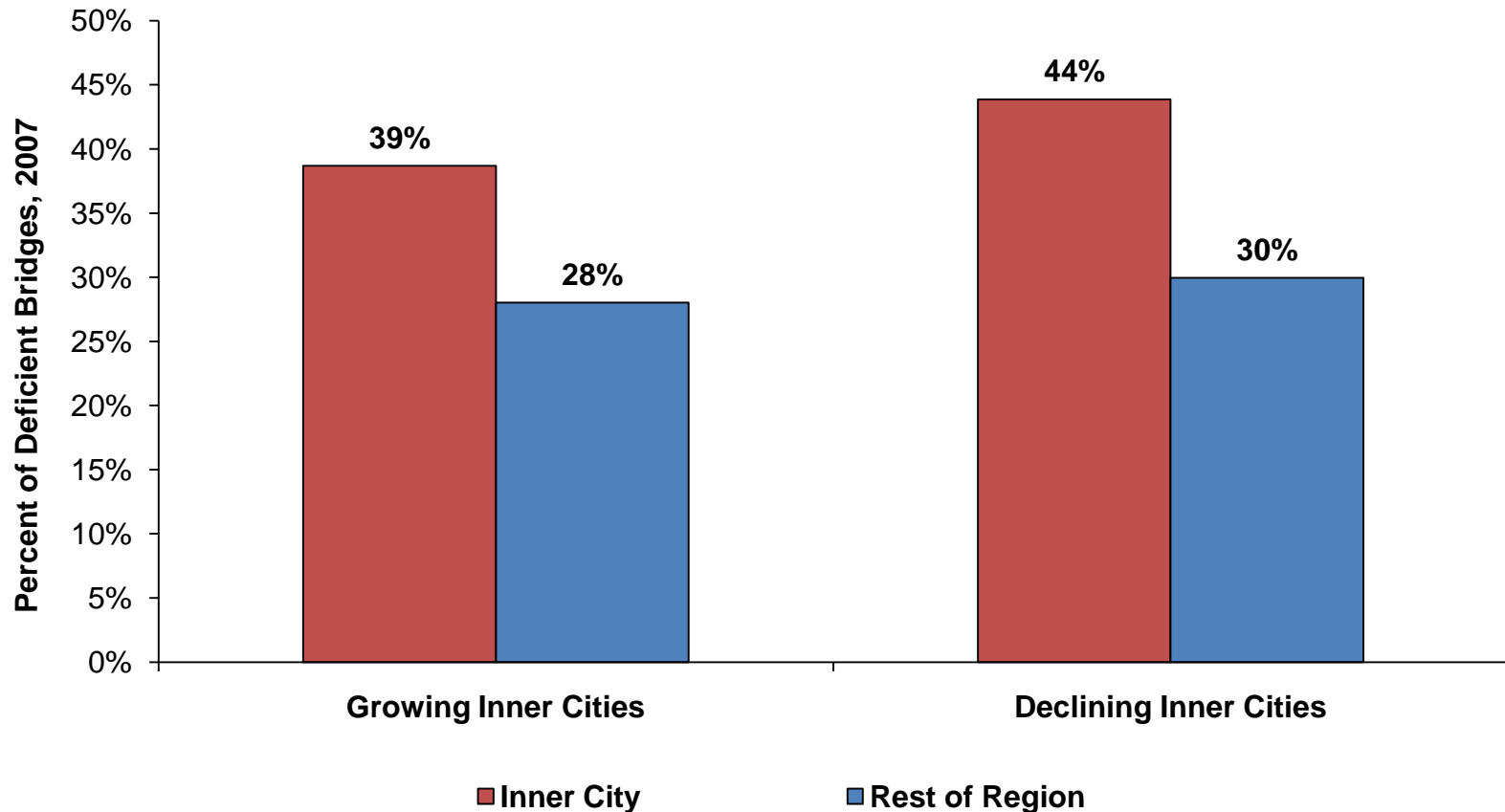
Transportation Infrastructure Density, 2008



- Infrastructure density is an advantage of inner city location
- Distribution sector employment is disproportionately higher in the inner city

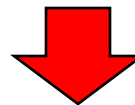
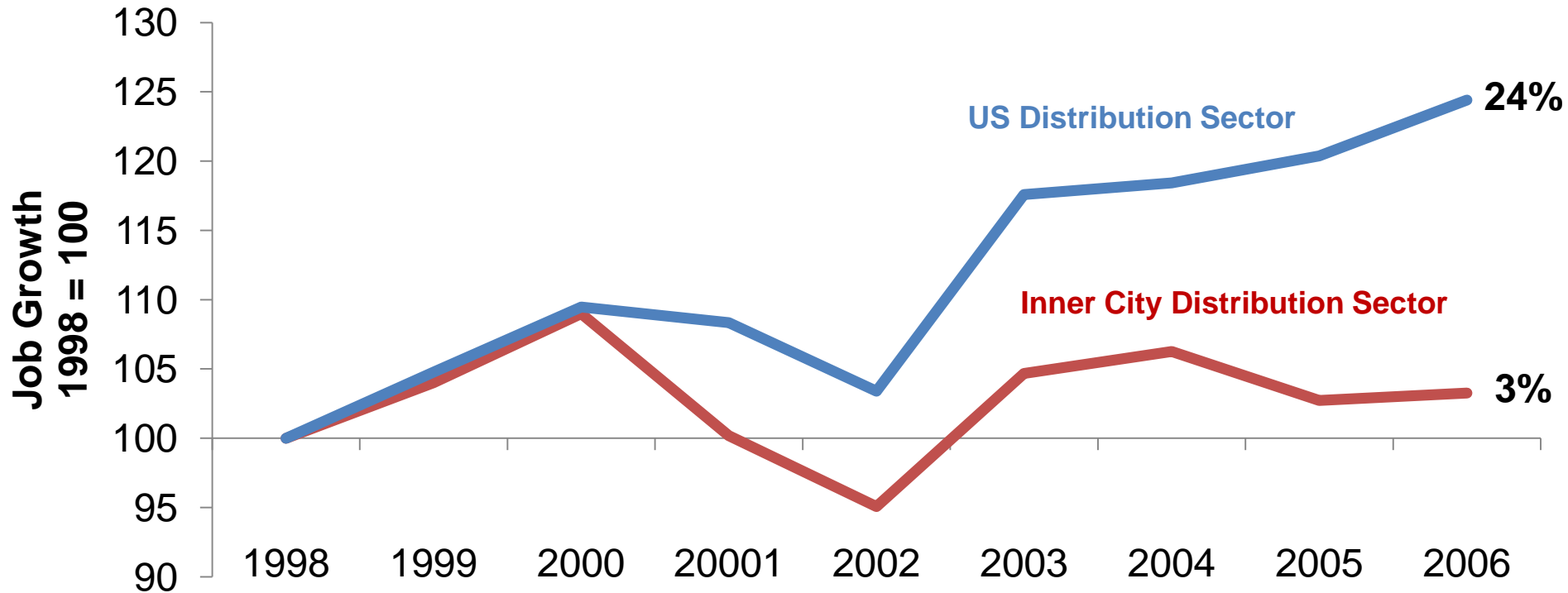


ICIC Business Environment: Infrastructure Quality



- When it comes to bridge quality, the only available proxy for infrastructure quality, inner cities are in noticeably worse shape than their central cities and regions

Business Environment: Inner City Distribution Sector Employment Growth, 1998-2006

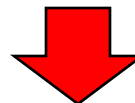
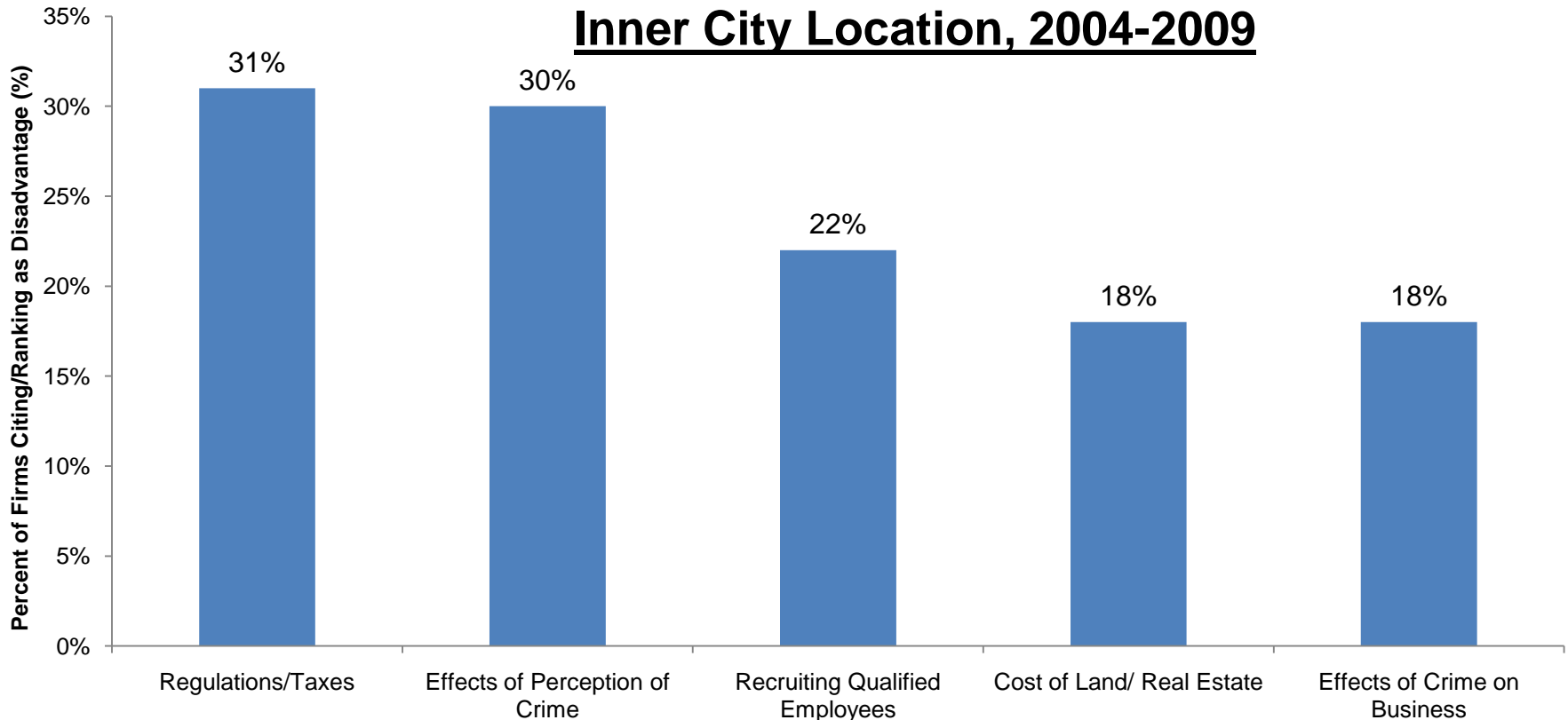


- Despite the benefits of infrastructure density within the inner city, **deteriorating infrastructure quality** is eroding this advantage over time



ICIC Business Environment: Disadvantages of Inner City

Most Cited/Highest Ranked Disadvantages to Inner City Location, 2004-2009

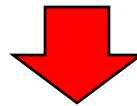
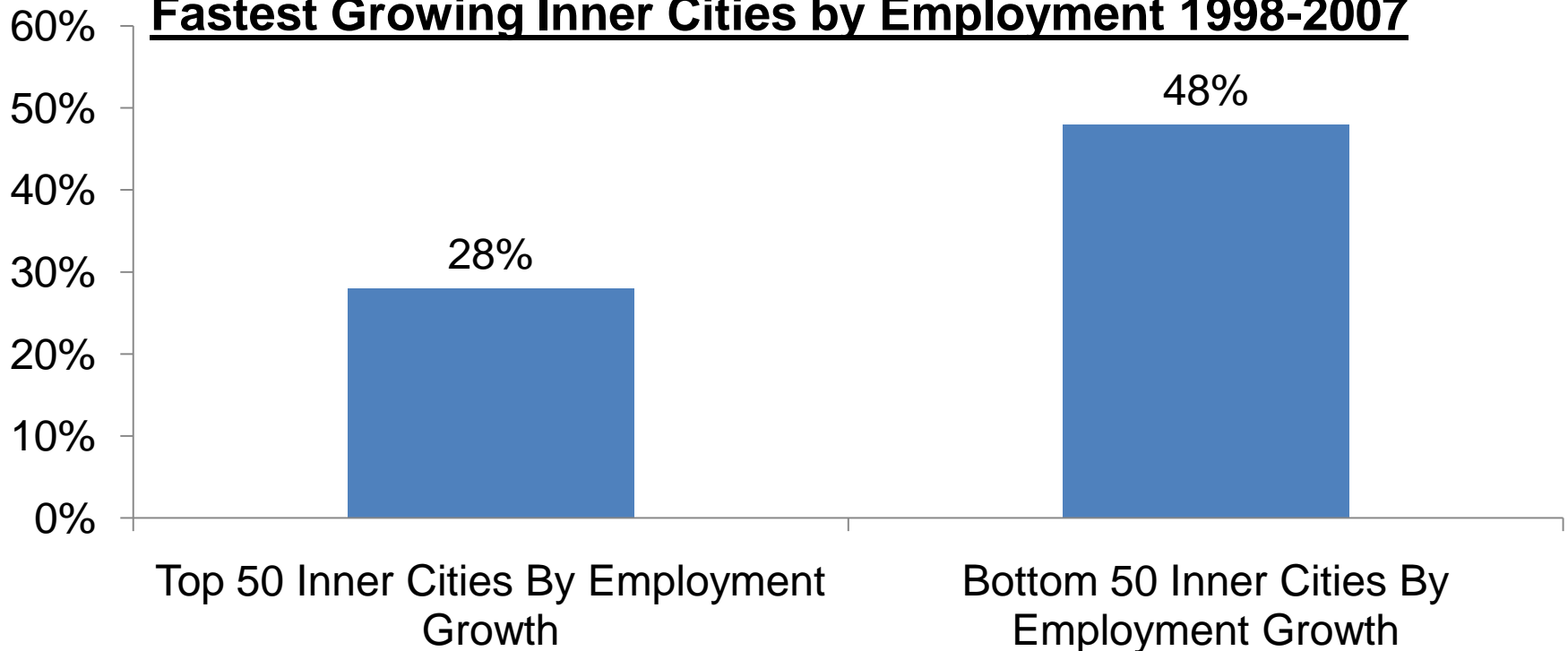


- **Regulations** and the **perception of crime** are the most cited disadvantages of doing business in the inner city

Source and Notes: ICIC analysis of Inner City 100 Survey data, 2004-2009, n=504. Respondents chose up to 3 factors out of a list of 10. (2004-2006) or ranked 1 or 2 on scale of 1 to 7 (2008-2009).

Business Environment: City Growth and Number of Inner City 100 Companies

Percent of Inner City 100 Firms Located in Top vs. Bottom 50 Fastest Growing Inner Cities by Employment 1998-2007

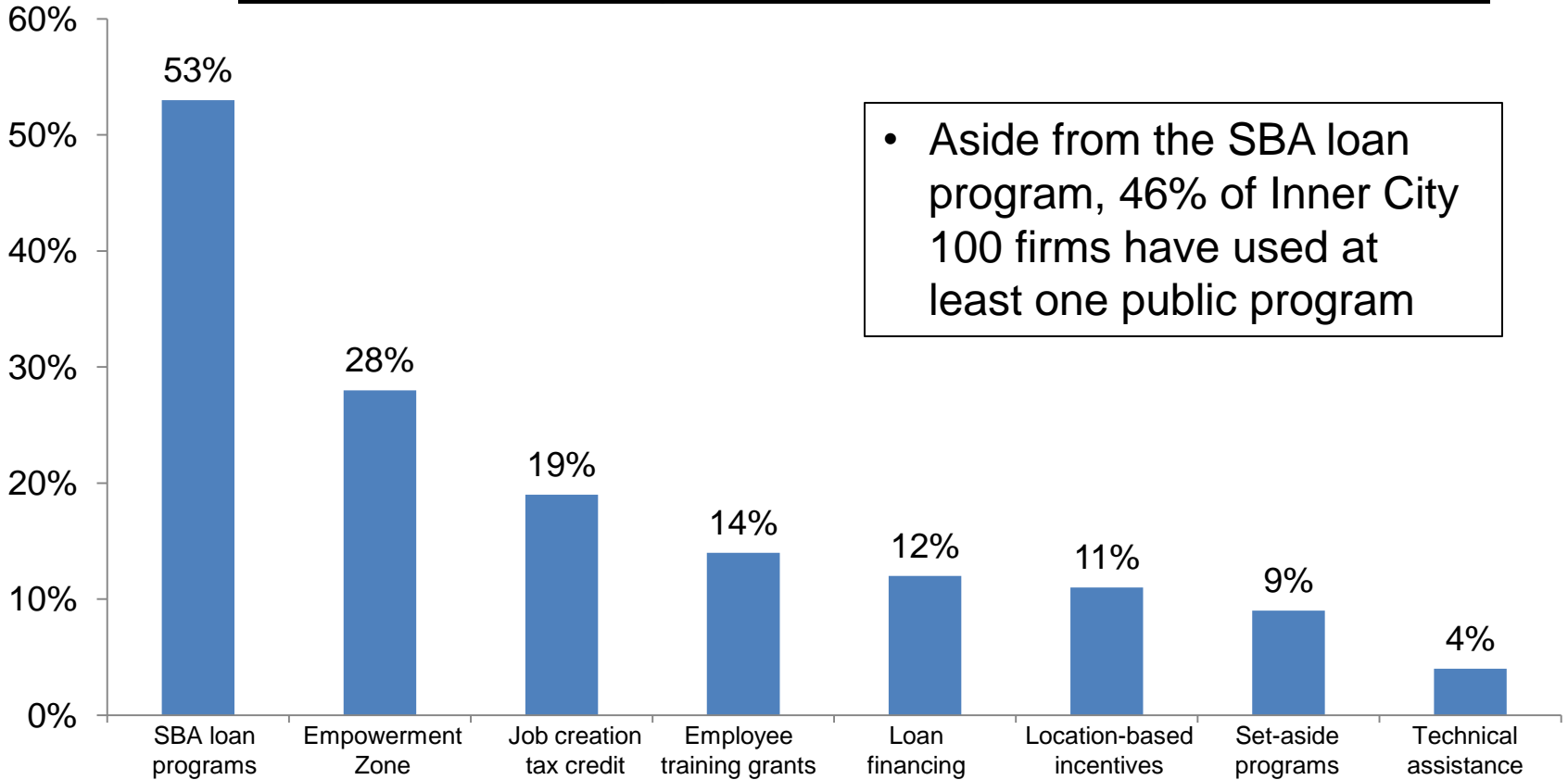


- Location matters but **does not fully determine success** as growing inner city companies succeed in both advantageous and disadvantageous environments



ICIC Business Environment: Use of Public Programs

Use of Public Programs by Inner City 100 Firms, 2006



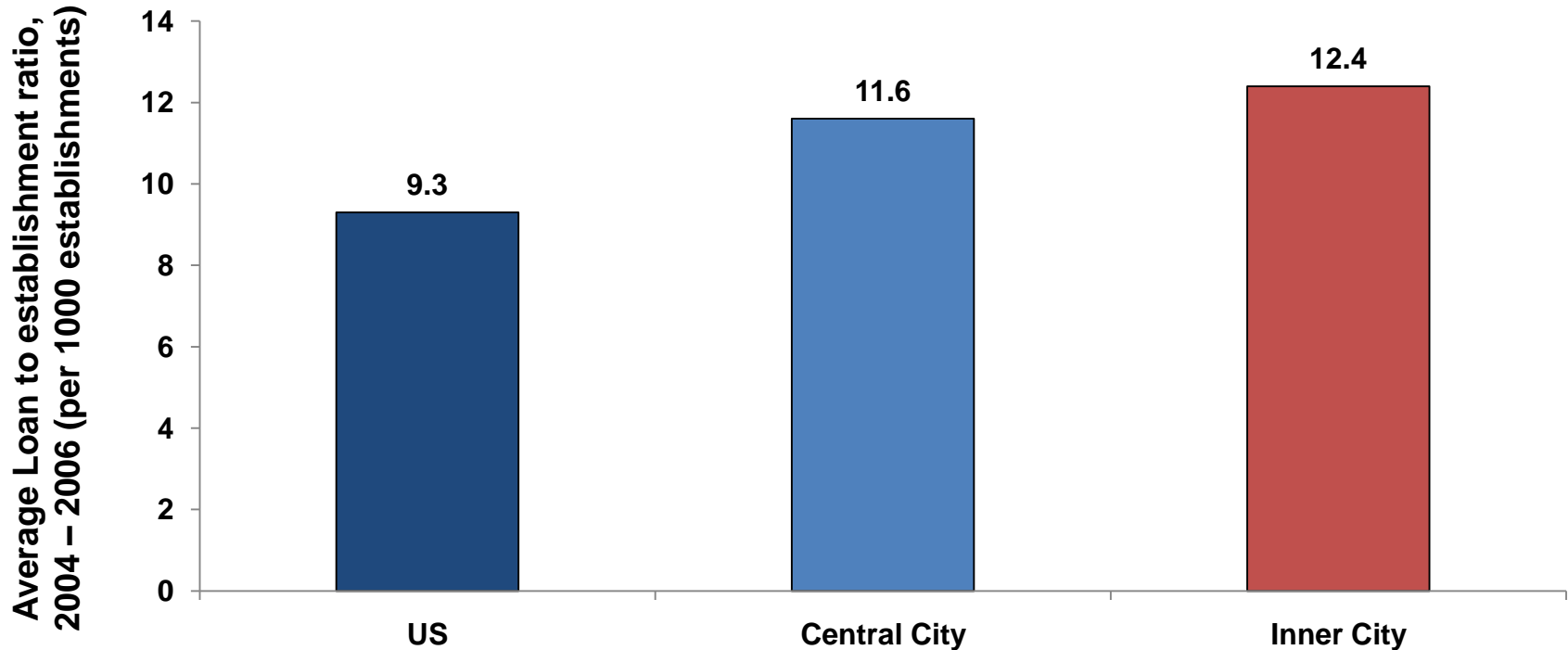
- Aside from the SBA loan program, 46% of Inner City 100 firms have used at least one public program



- **SBA loans, empowerment zone** and **job creation tax credits** are the most often used public programs by Inner City 100 firms

Public Programs: Use of SBA Loans

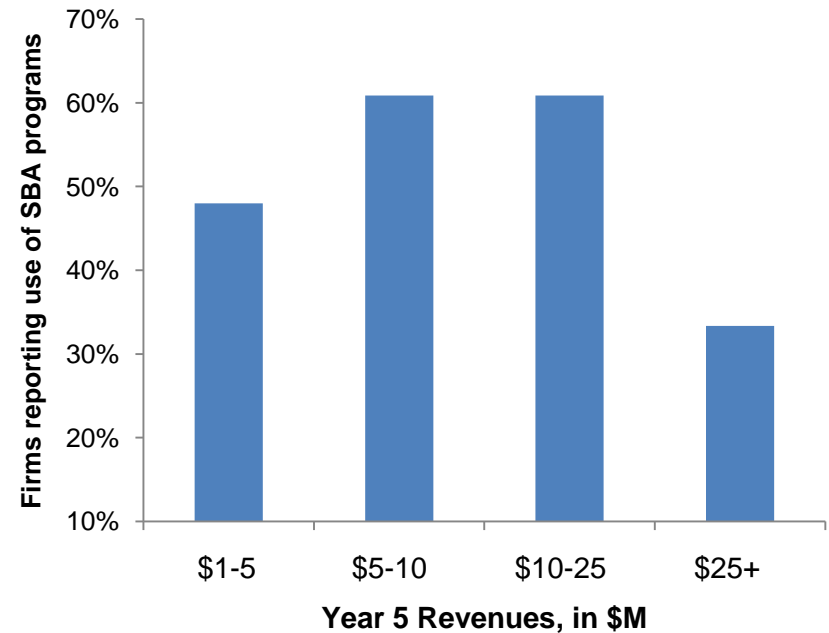
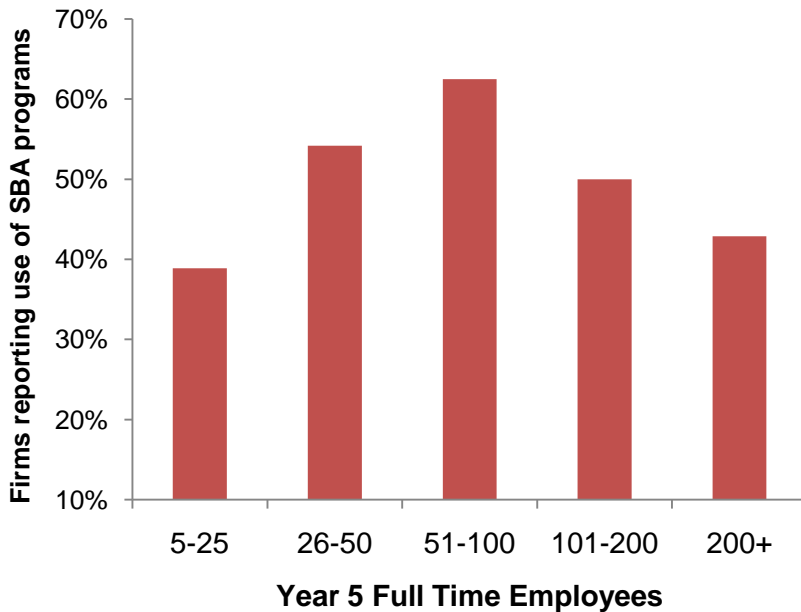
Higher SBA Loan Representation in the 100 Largest Inner Cities vs. Rest of Central City and the US, 2004 -2006



- Firms in inner cities have a higher concentration of SBA loans

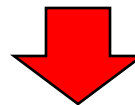
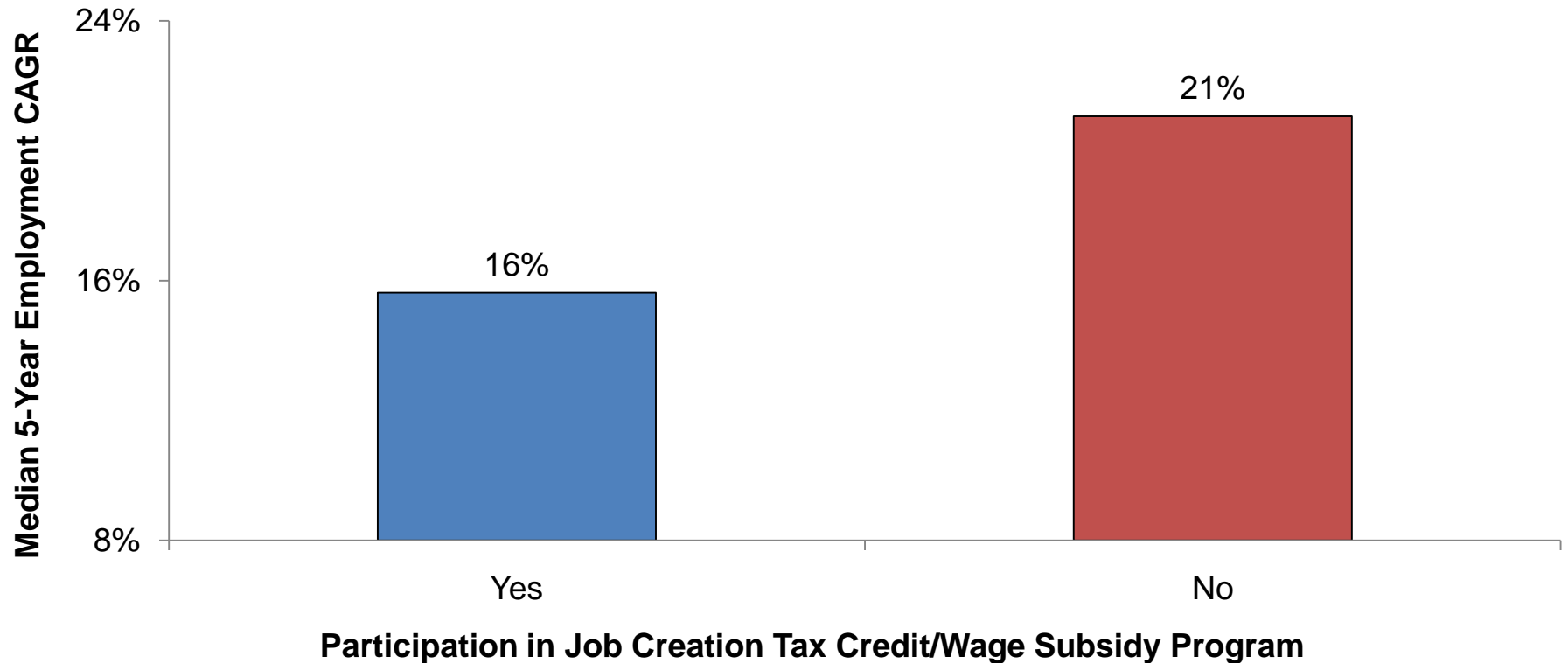
Public Programs: Inner City 100 Use of SBA Programs by Size of Firm

Use of SBA Programs by Inner City 100 Firms, 2007



- A higher percentage of firms that take advantage of SBA programs have already achieved some **critical mass**

Public Programs: Impact of Job Creation Tax Credits/Wage Subsidies on Employment Growth



- Inner City 100 firms who took advantage of job creation tax credits and wage subsidies **did not generate higher job growth**

Summary: Inner City Business Environment

“Frankly, we hope that our competitors never catch on to the value of the assets which exist in the inner city... the talented pool of people, the access to the infrastructure of transportation... create a set of resources that are unmatched any place else. But please, don't tell our competitors that.”

-CEO of a Technology Manufacturing Company

- Transportation-heavy industries are overly represented in the Inner City 100, however deteriorating infrastructure is weakening the inner city advantage
- City growth matters but does not determine individual firm success
- Public programs matter, especially the SBA
- SBA programs are most heavily utilized by firms that have already achieved some growth
- Job creation tax credits and wage subsidies are not generating higher job growth among Inner City 100 firms who use them



ICIC Factors Influencing the Growth of Inner City Firms

Financing

- Access to Capital
- Sources of Capital

Inner City Business Environment

- Advantages
- Disadvantages
- Use of Public Programs

Company Revenue Sources

- Customer Mix
- Government Contracts

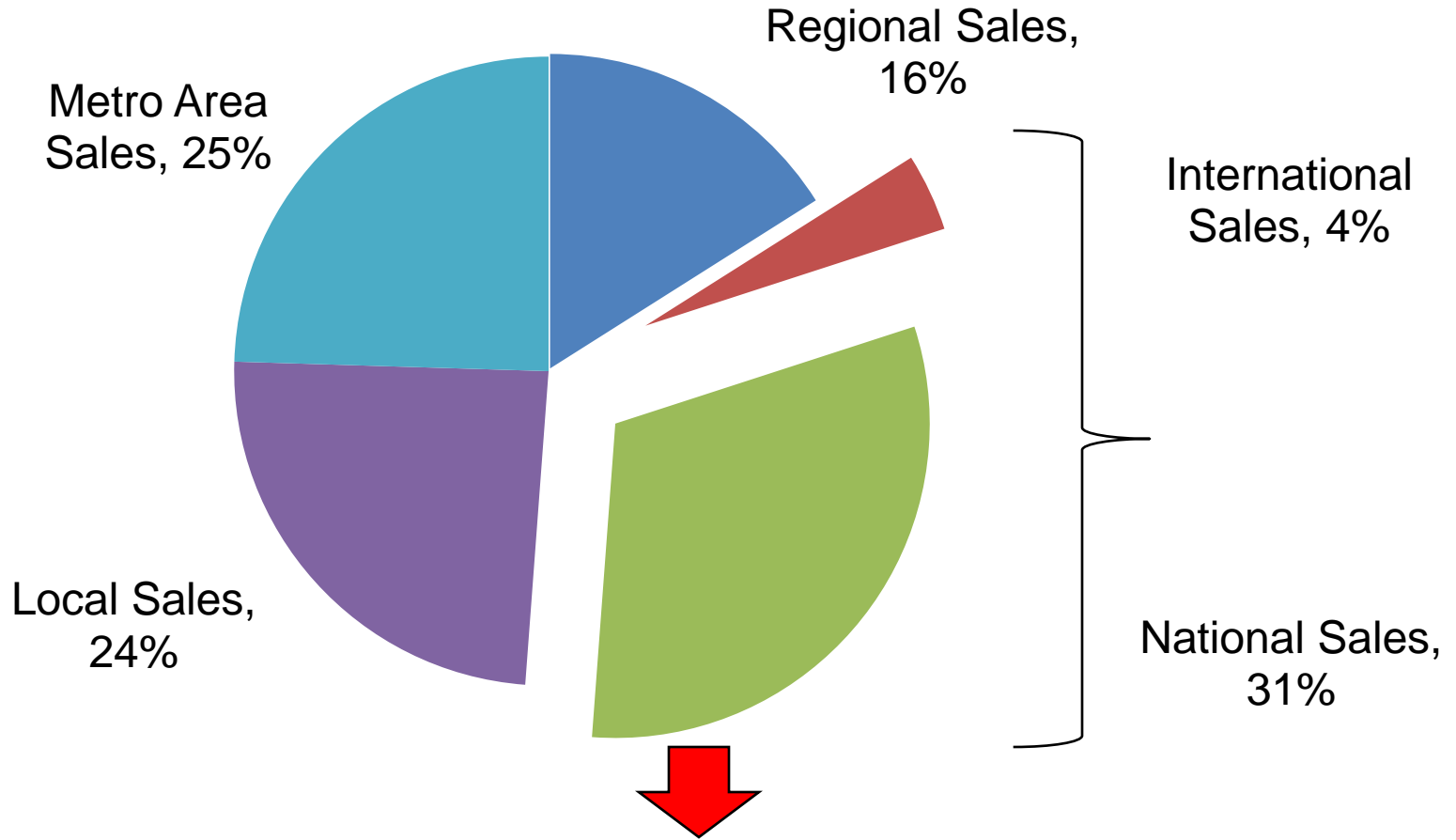
Leadership and Human Capital

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ICIC Revenue Sources: Inner City 100 Customer Base

Inner City 100 Sales by Customer Location, 1999-2009

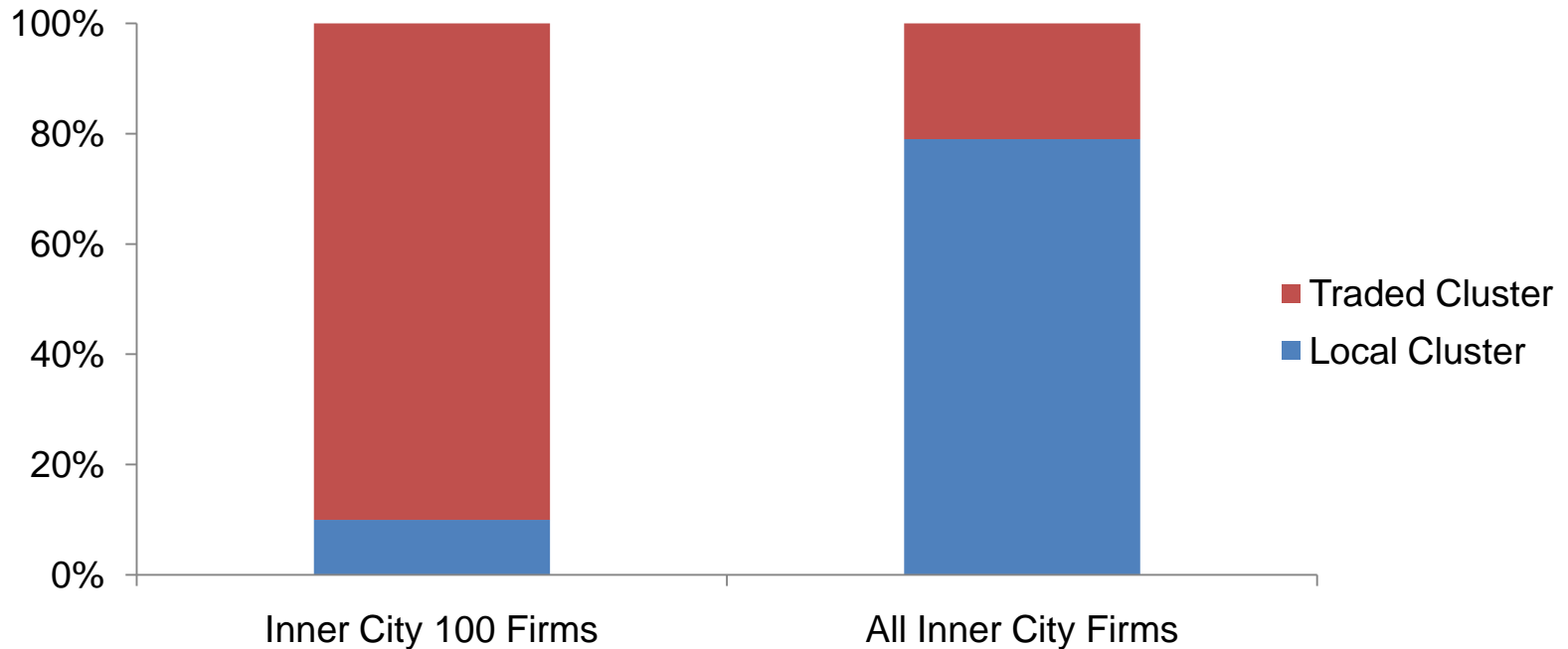


- **National and international sales** represent a significant portion of Inner City 100 firms' sales



ICIC Revenue Sources: Inner City Firms in Traded vs. Local Clusters

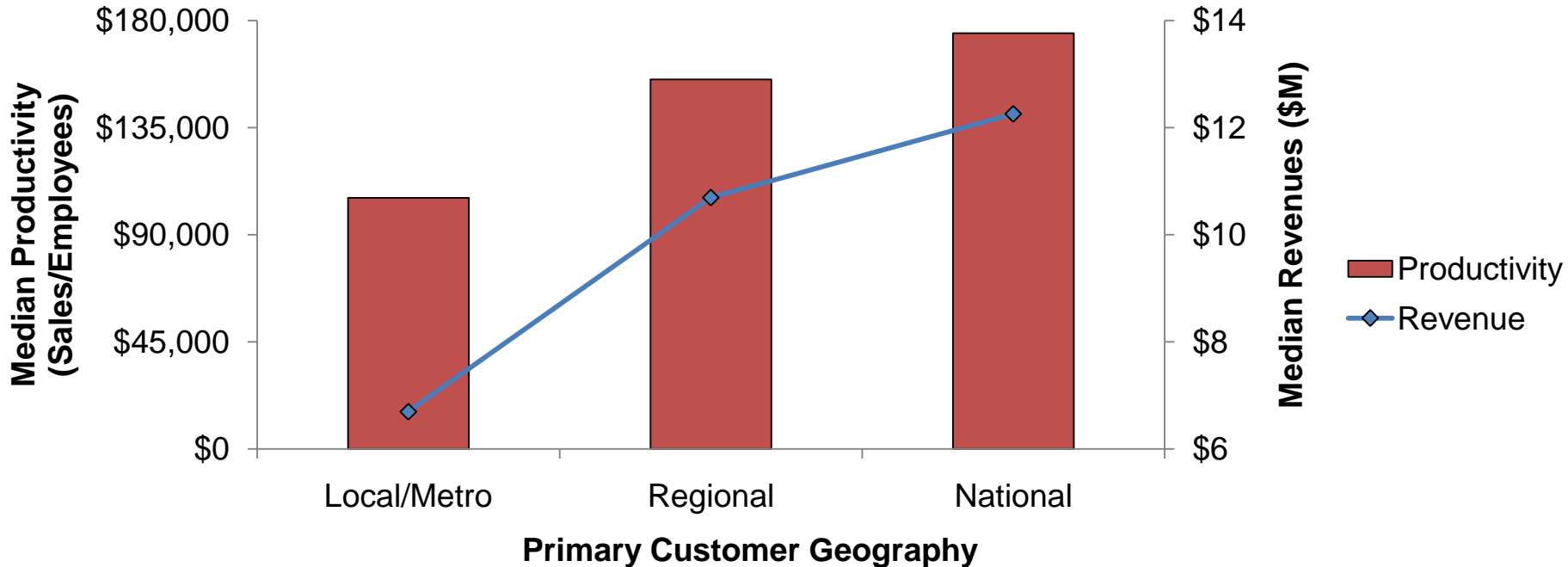
Percentage of Inner City Firms, 1999-2009



- While the overwhelming majority of inner city firms belong to local clusters, Inner City 100 firms are heavily skewed toward **traded clusters**

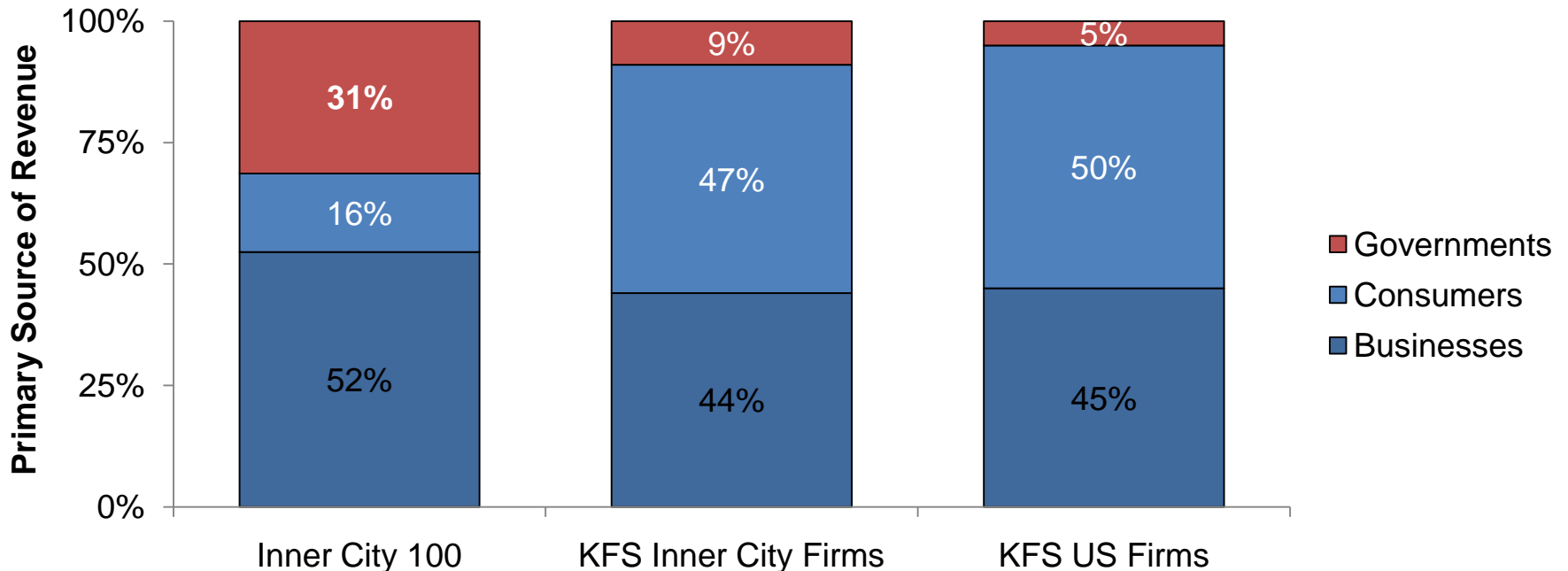
Revenue Sources: Impact of Customer Geography on Business Productivity

Inner City 100 Productivity and Revenues by Primary Geographic Customer, 1999-2009



- Inner City firms, with a broader customer scope, typically have **higher revenues and median productivity per employee**

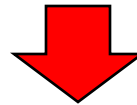
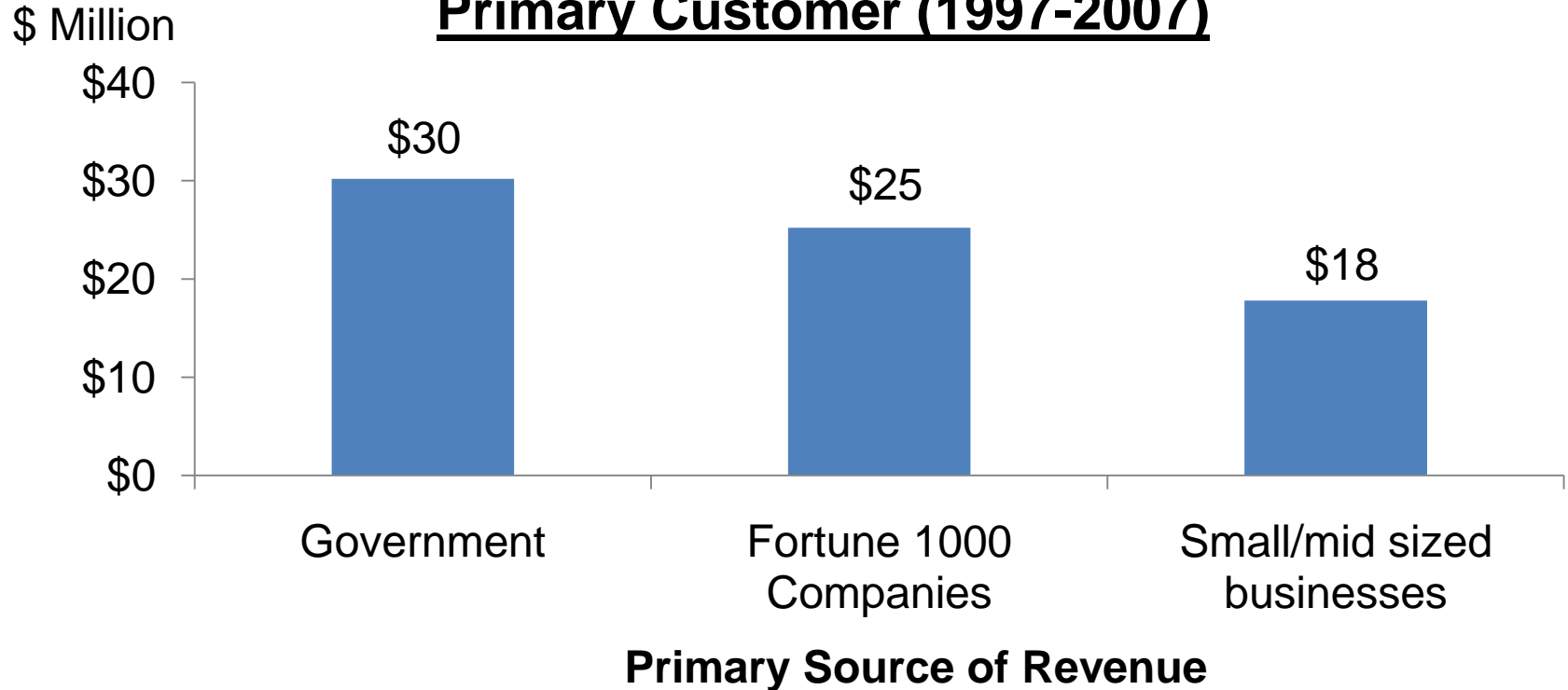
Customer Mix Comparison between Inner City 100, US Inner City Firms, and Total US, 2004-2006



- The government is a **major source of revenue** for fast growing inner city businesses

Revenue Sources: Average Firm Size by Primary Customer

Average Annual Revenue for Inner City 100 by Primary Customer (1997-2007)



- Inner City 100 firms identifying the government as their primary source of revenue have higher average revenues

Revenue Sources: Summary

“Our first government contract was landed in 1999. We rely on a mix in terms of government contract size, with some contracts being quite large and others small. These contracts are often a great source of stability. They can be quite large (up to several millions of dollars) and continue on for years, providing a reliable, steady source of revenue.”

-CEO of a Management Consulting Firm, 2009 ICIC Interview

- Inner City 100 firms with a more geographically diverse mix of sales typically have higher median revenues and productivity per employee
- Inner City 100 firms have leveraged government contracts to achieve greater size and scale



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- Sources of Capital

Inner City Business Environment

- Advantages
- Disadvantages
- Use of Public Programs

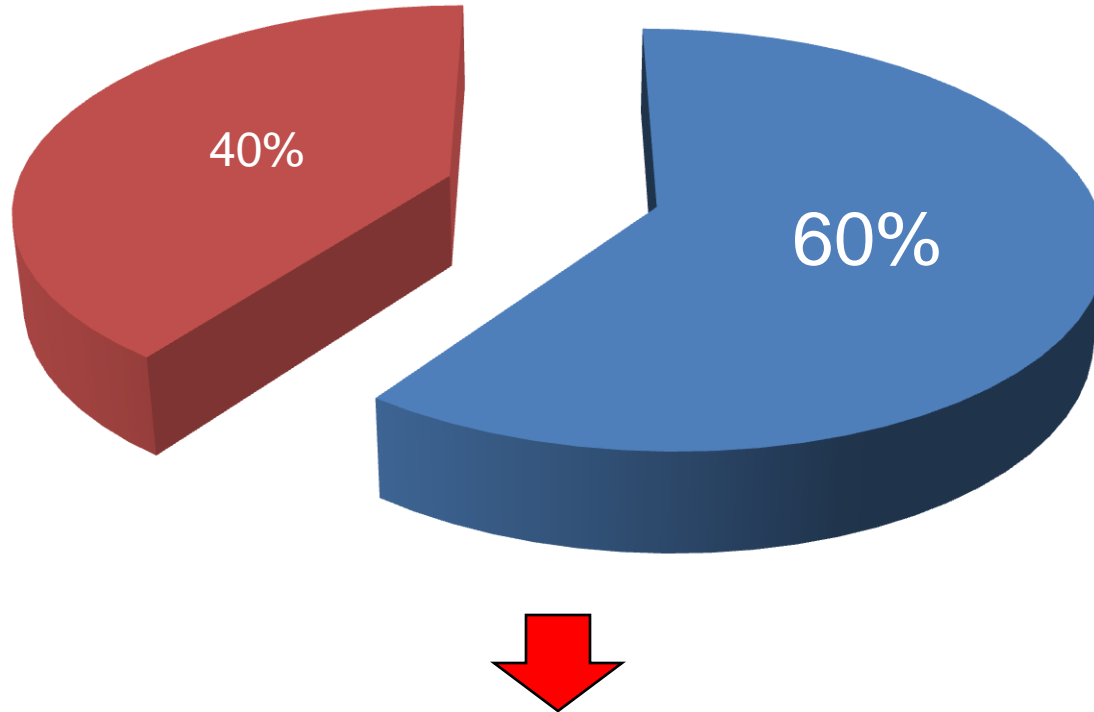
Company Revenue Sources

- Customer Composition
- Customer Location

Leadership and Human Capital

- CEO Background
- Inner City Workforce
- Employee Benefits and Training

Percentage of Inner City CEOs with a Family History of Business Ownership, 1999-2009

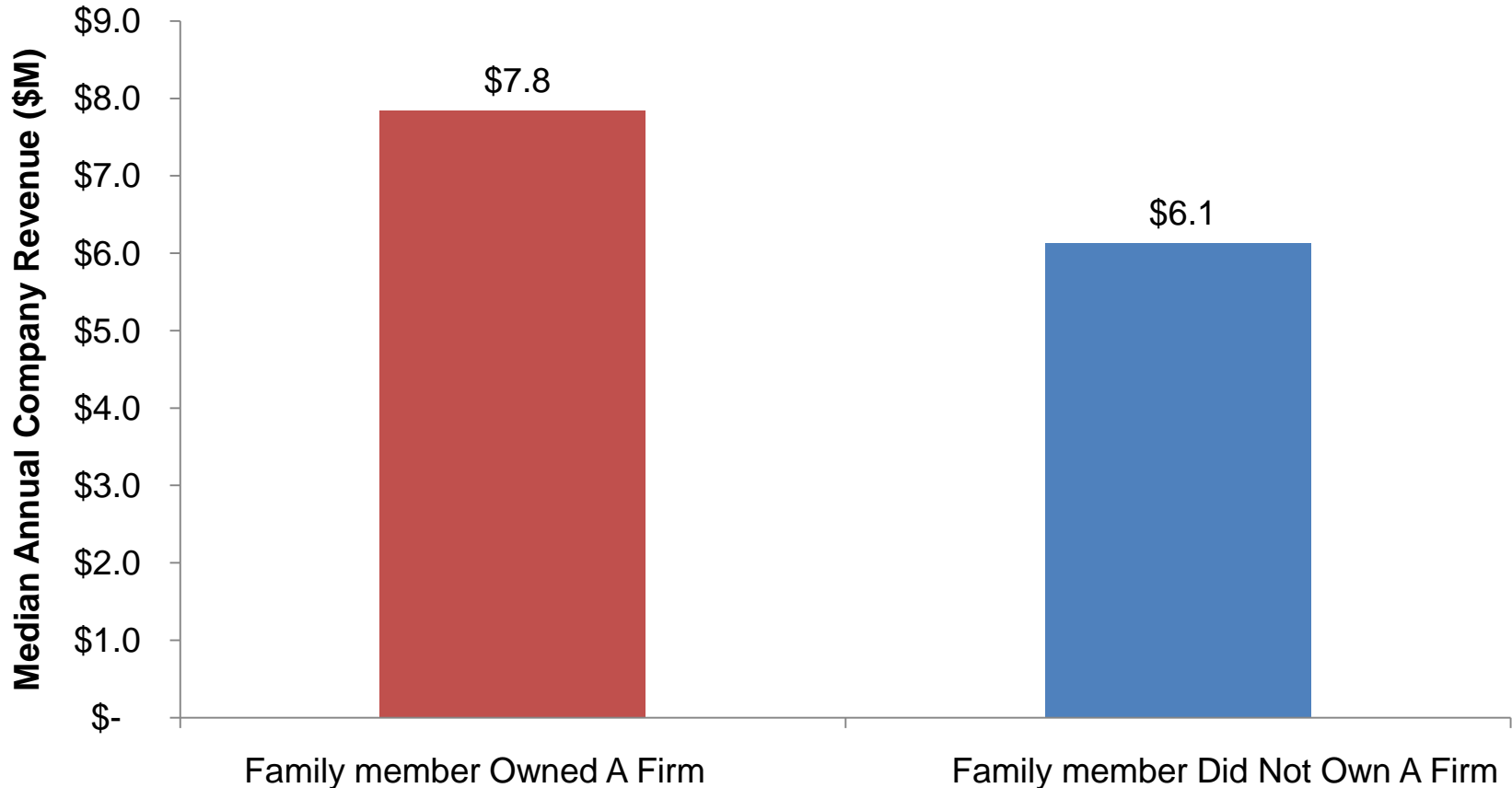


- 60% of Inner City CEOs had a close family member who owned a business while they were growing up



ICIC Leadership: Family Background in Entrepreneurship

CEO Family Background in Entrepreneurship, 1997-2007

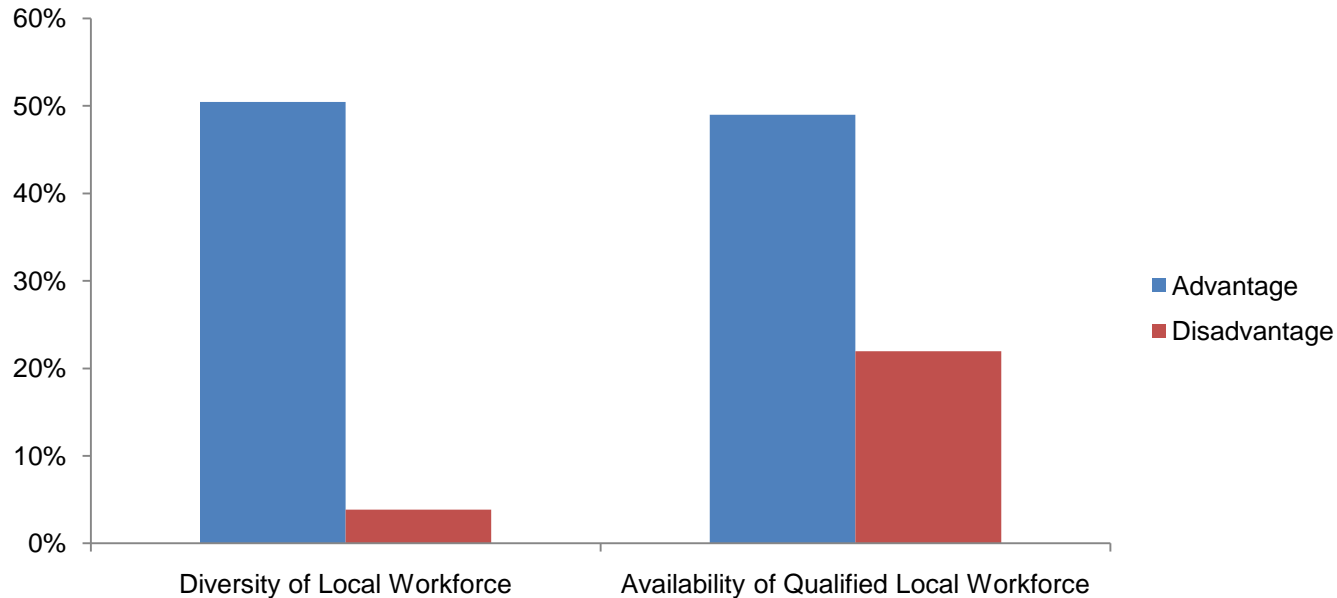


- Firms with CEO's with a family history of business ownership are **larger**



ICIC Workforce: Advantages and Disadvantages of the Inner City Workforce

Average Percent of Inner City 100 Firms Rating Workforce as Advantage or Disadvantage to Inner City Location, 2004-2009

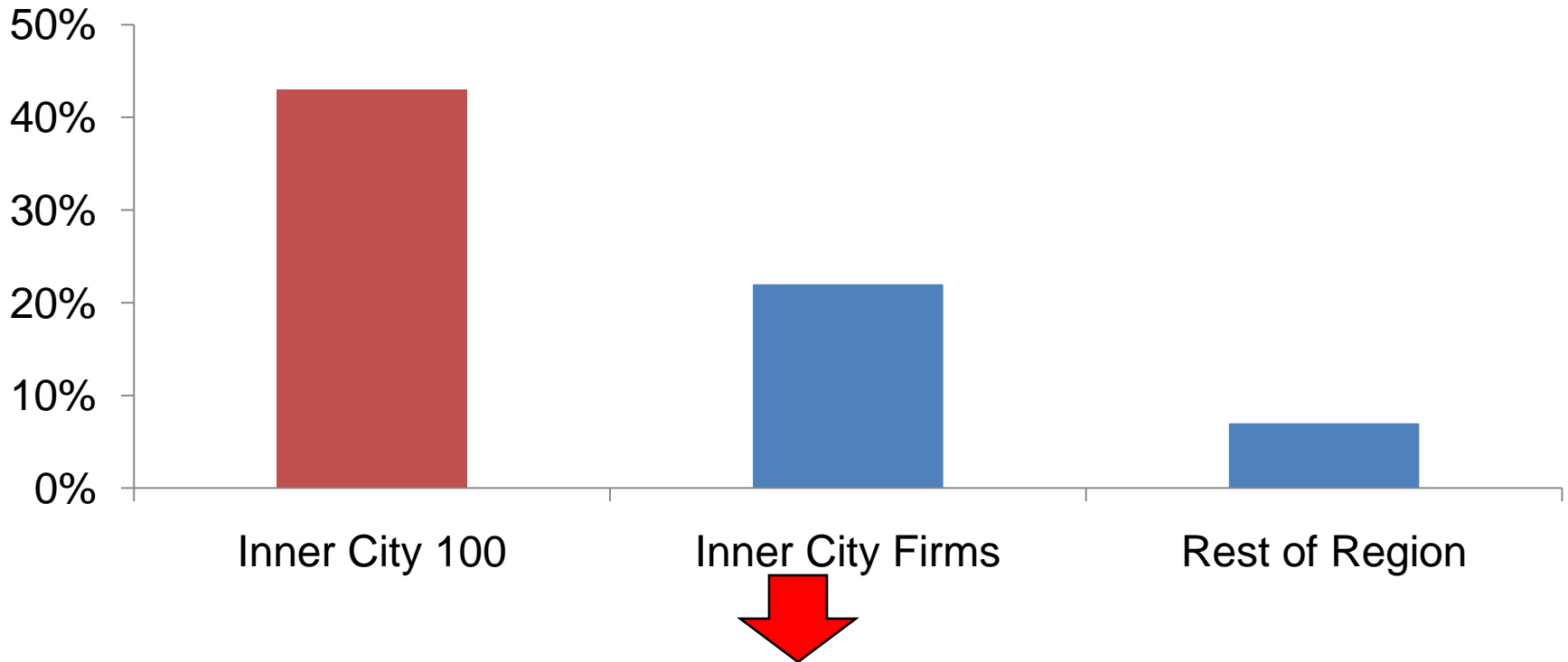


- Inner City 100 firms predominantly see the local workforce as an **advantage**



ICIC Workforce: Employment of Inner City Residents

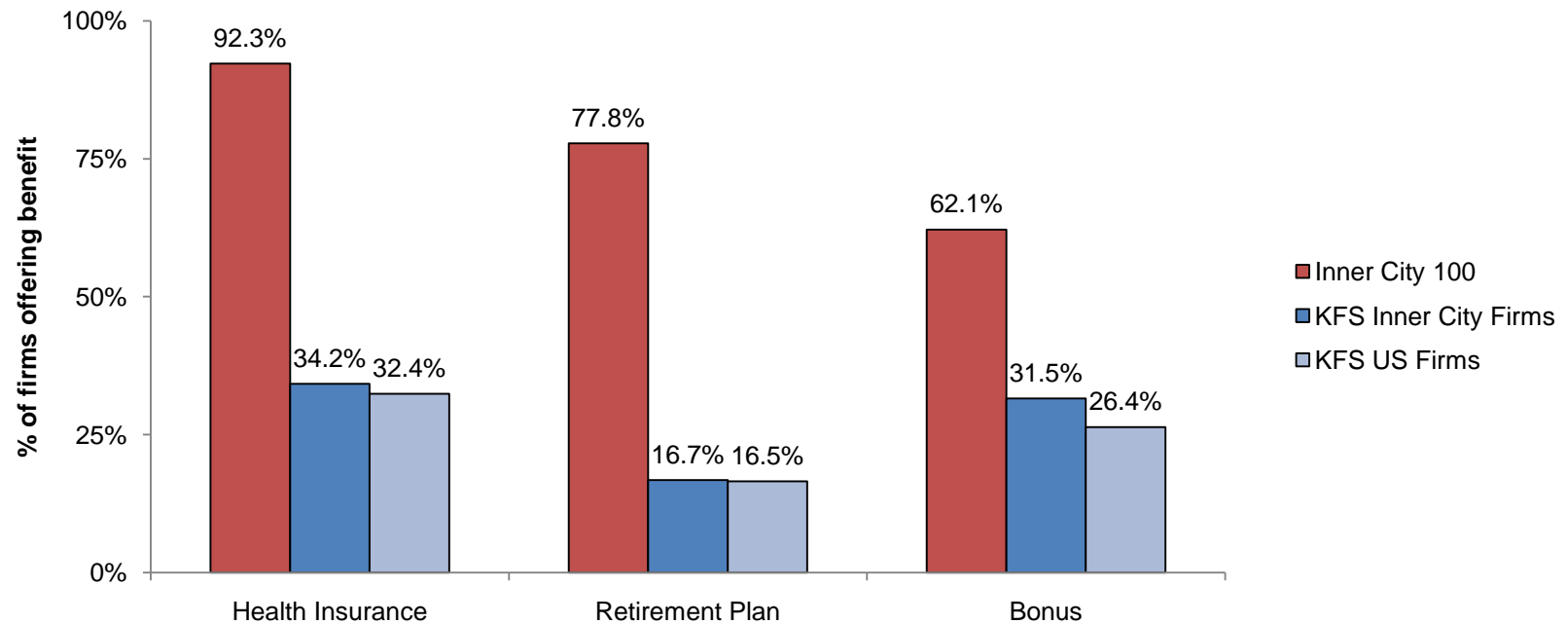
Percentage of Employees Residing in the Inner City



- Growing inner city firms hire **nearly twice as many local inner city residents** as a percent of their total employees as other inner city firms, and **6 times** the regional average

Workforce: Benefits and Training

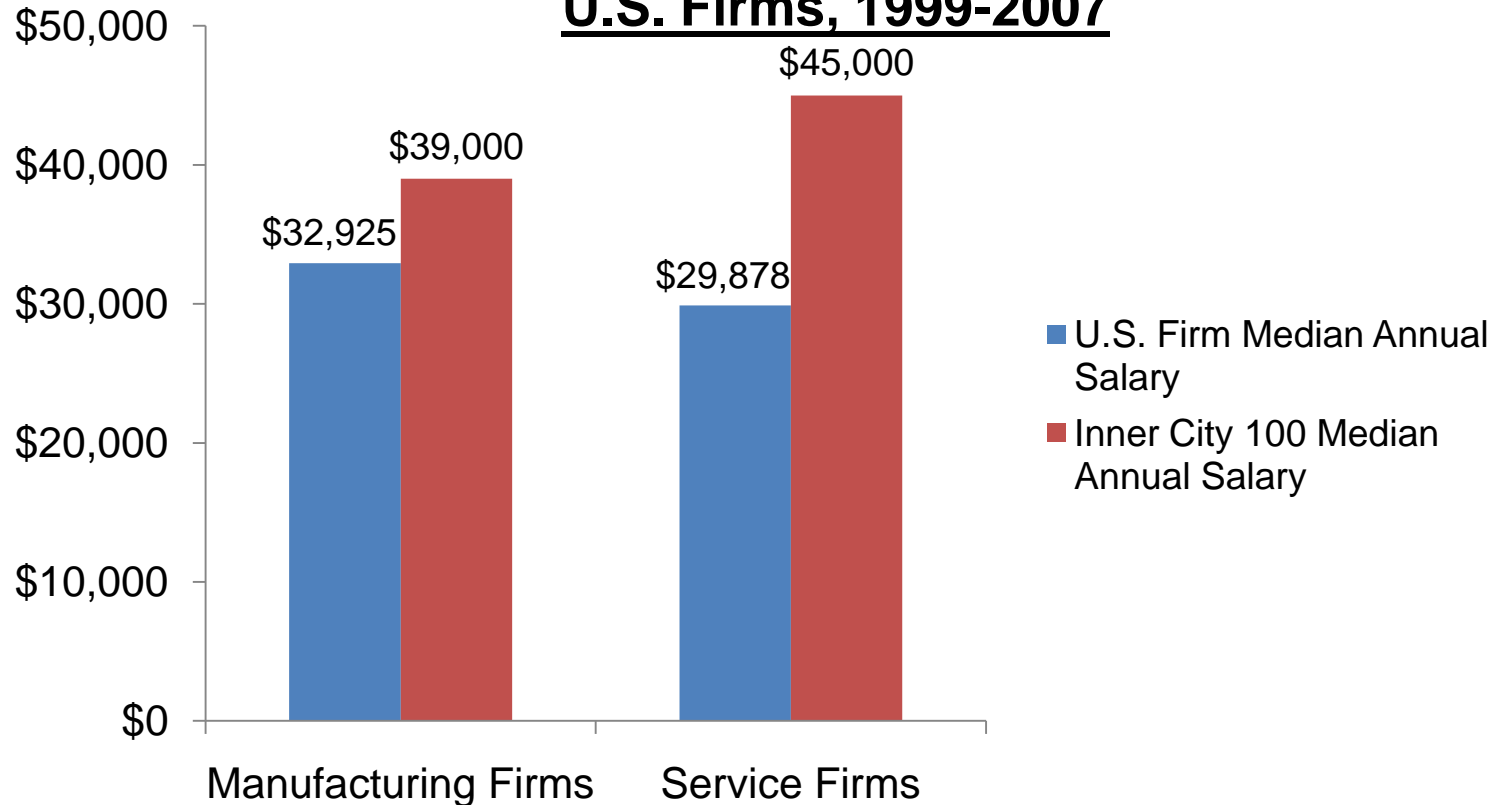
Employee Benefits Offered by Inner City 100 vs. Inner City and US Firms



- A higher percentage of Inner City 100 firms **offer benefits** than their peer firms in inner cities and the US, independent of firm size

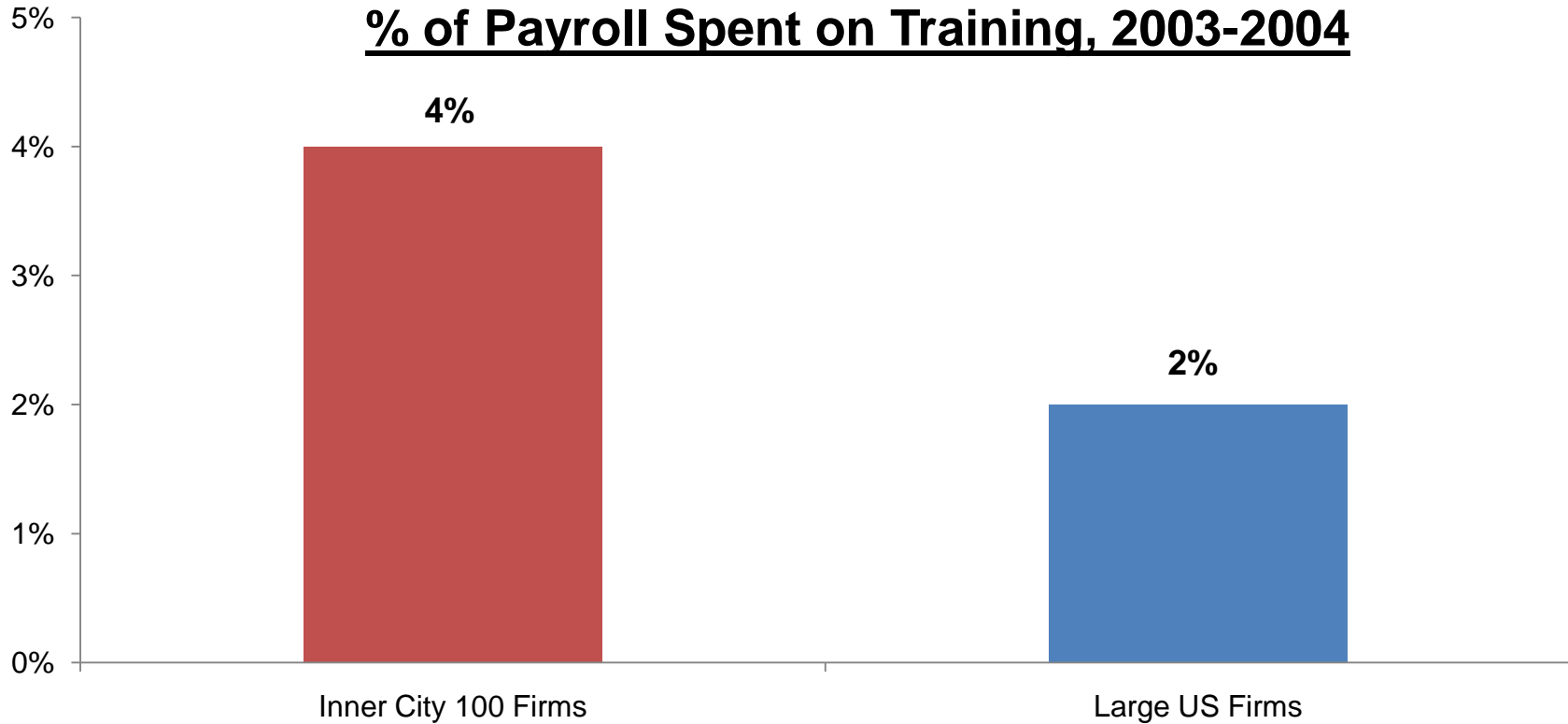
Workforce: Annual Salaries

Median Annual Salary for Inner City 100 vs. U.S. Firms, 1999-2007



- Inner City 100 manufacturing and service firms pay employees higher salaries than US firms overall

Workforce: Spending on Training

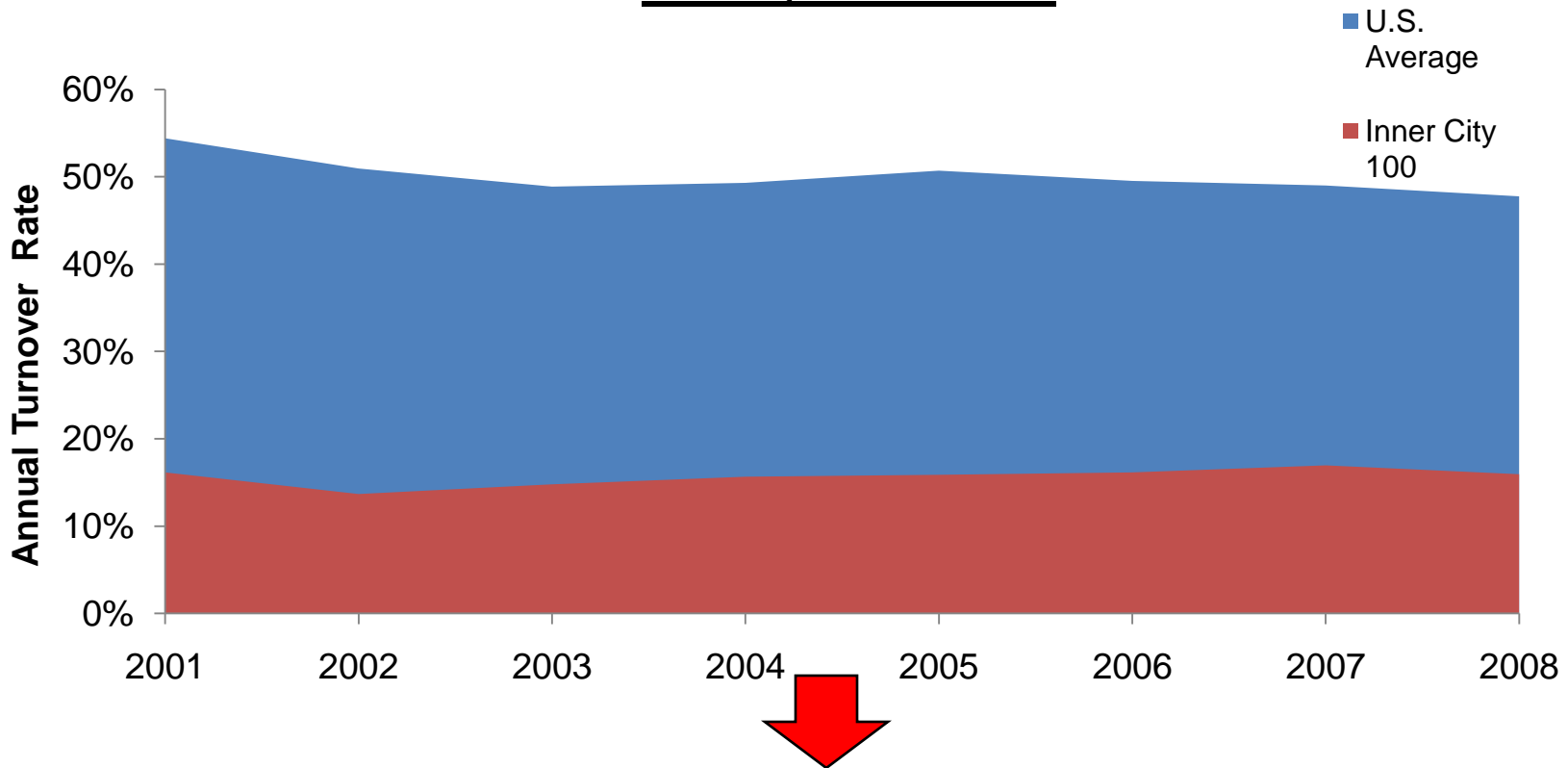


- Inner City 100 firms spend approximately **twice as much** of their total payroll annually on training as large corporations in the US

Source and Notes: ICIC analysis of Inner City 100 Survey data, 2003 and 2004; n=195

*According to the 2004 ASTD (American Society of Training and Development) survey of more than 375 major corporations, firms spend 1-3% of total annual payroll on training.

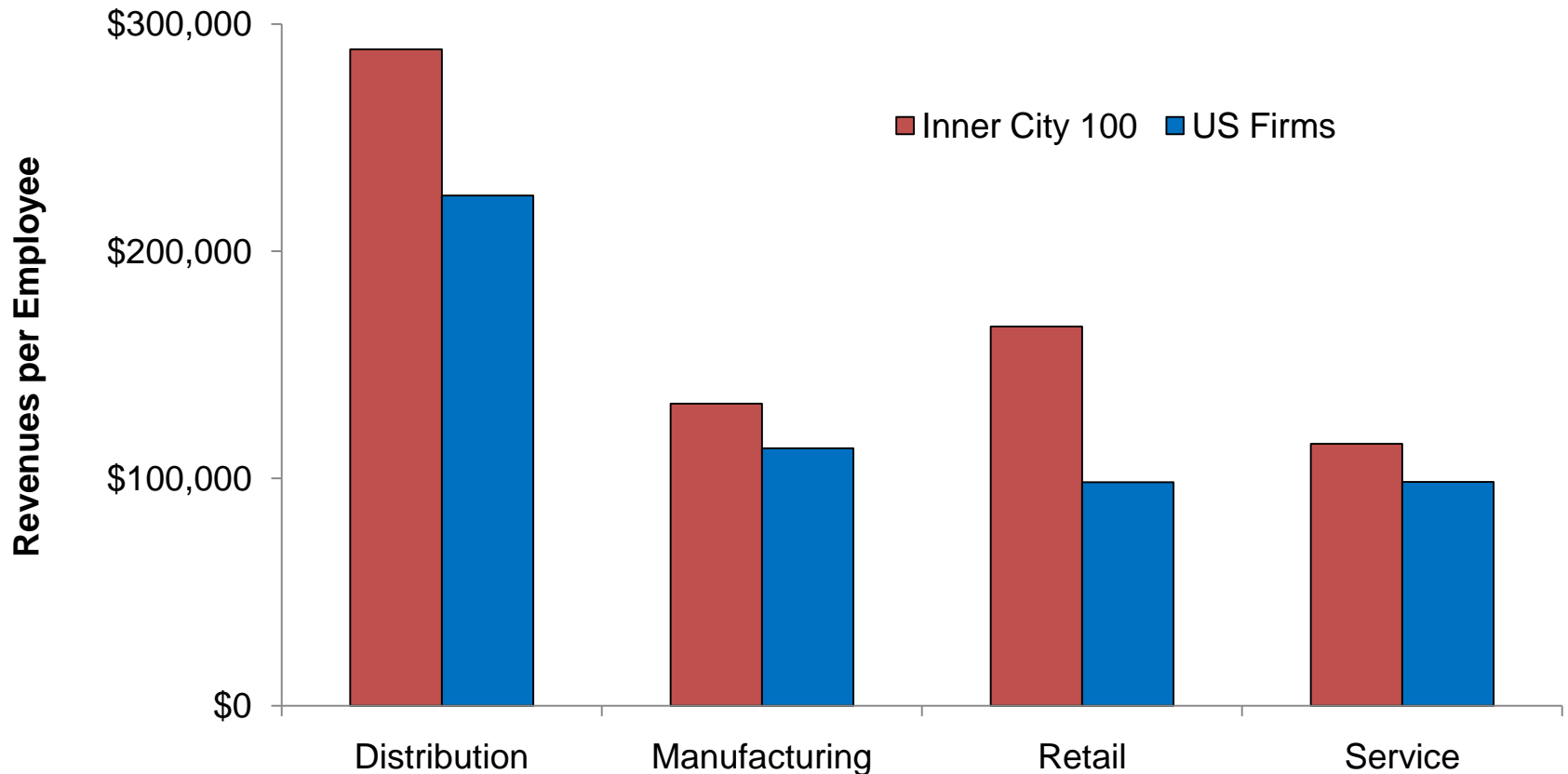
Average Employee Turnover Rate, Inner City 100 Firms vs. US Firms, 2001-2008



- Turnover rates in Inner City 100 firms are **significantly lower** than the national average

Workforce: Impact on Firm Productivity

Revenue per Employee By Sector, Inner City 100 vs. US Firms



- Inner city 100 firms are **more productive** than their sector peers in the US overall

“Everything in business is about the employees. Employees respond very well to benefits. The company simply cannot recruit without a strong benefits package. The most talented people have a number of competitors that they could go to.”
- CEO of a Technology Company

- A family history of business ownership has benefited Inner City 100 CEOs
- Inner City 100 firms are leveraging the advantages of the local workforce by hiring a higher percentage of inner city workers
- Inner City 100 firms spend more on training, pay higher wages and offer more benefits than other businesses, achieving lower turnover rates and higher productivity rates

Agenda

- Why Are Fast-Growing Firms in the Inner City Important?
- Project Methodology
- Characteristics of Fast-Growing Inner City Firms
- Factors Influencing Growth
- Implications for Firms and Policymakers

Selected Findings

- *Finding #1:* Inner City 100 firms **hire more local inner city residents** and spend more on **employee training**, generating **lower turnover** and **higher productivity**
- *Finding #2:* **SBA loan products are heavily used** by successful inner city firms, especially firms with more than 25 employees
- *Finding #3:* Inner City 100 firms whose primary source of revenue is the **government** seem to have used these **contracts to scale** their businesses
- *Finding #4:* **Limited access to capital** and a heavier **reliance on debt** for growth have impeded Inner City 100 firms from achieving the same **scale and growth** as comparable U.S. firms
- *Finding #5:* **Early exposure to entrepreneurship** has a positive impact on firm success

Selected Implications for Firms

- Implication: Capital markets do not seem to be addressing the inner city business market well. SBA programs are filling some of this need

Recommendations:

- Be creative about leveraging payment terms with suppliers and factoring receivables to manage working capital needs without impacting growth
- Look for alternative sources of financing such as social venture capital or double-bottom-line funds, and take advantage of SBA loan programs
- New private sector financing models are needed to assess inner city risk and offer new debt products with deferred repayment features to avoid the trade off between cash flow and growth

- Implication: Government contracts tend to provide a more stable base of revenue from which inner city firms can grow

Recommendation:

- Devote resources to generating sales from government sources

- Implication: To get the most out of the inner city workforce, training, benefits and competitive compensation is critical

Recommendations:

- Offer competitive salaries and benefits and invest in training to reduce turnover and increase productivity
- Provide employees with an opportunity to give back to their local communities

- Implication: Utilizing the local workforce can result in greater employee loyalty and productivity

Recommendation:

- Recruit employees from the local inner city community

Selected Implications for Policymakers

- SBA loan programs are important for inner city firms and are most utilized by companies that have already achieved some scale

Recommendations:

- Reduce red tape and transaction costs for SBA loans which hinder some smaller firms from taking advantage of the programs
- Expand maximum SBA loan size
- Recapitalize and refocus existing 8a and SBIC programs that target businesses in distressed communities
- Fund new location-based programs with more effective business models

- Implication: Government contracts can be a significant part of getting inner city business to scale

Recommendation:

- Local, state and federal governments should weight inner-city location targets in their procurement programs
- New opportunities to improving public procurement in inner cities will pay big dividends
- Government should encourage educational and health care anchors in inner cities to purchase locally

- Implication: Training is important, especially for a more diverse employee base

Recommendations:

- Link training to clusters
- Orient training providers towards economic development and the needs of business
- Allow flexibility and experimentation at the local level
- Place training service centers near target populations
- Create better mechanisms for matching of residents to regional and inner city jobs
- Include “work readiness” programs
- Prepare lower-skilled workers for “middle-skilled” jobs

Q&A