Entrepreneurship

The U.S. economy’s remarkable resilience in the face of shocks arguably owes to an array of institutions and policies that reward entrepreneurial activity. A competitive market system, a sound legal framework that secures property rights, a robust financial system, monetary stability, low inflation, and generally flexible labor markets encourage new business start-ups. Together these ingredients act as an engine for sustainable long-run economic growth. In such an environment, entrepreneurs have strong incentives to develop new products and new technologies and to discover profit opportunities that ultimately direct society’s resources toward the most productive activities.

In the United States, entrepreneurship fosters small business growth. Firms with fewer than 500 employees represent about 99.7 percent of all firms and account for about half of all private nonfarm output and employment. As one would expect, the turnover among small firms is very high. In 2002, for example, 550,100 new firms were created and 584,500 firms closed down. Between 1999 and 2000, job creation by new or expanding establishments of small firms amounted to about 10.8 million employees, while job destruction at establishments that downsized or closed totaled about 8.3 million employees. The net change of 2.5 million employees in small firms, however, represented 75 percent of the net nonfarm employment change in the United States.1

Economists Steven Kreft and Russell Sobel argue that the key link between economic freedom—the combination of favorable legal institutions and tax and regulatory policies—and economic growth is entrepreneurial activity.2 While several studies have found that nations with higher economic freedom tend to have larger per capita income and higher rates of economic growth, Kreft and Sobel analyze entrepreneurial activity across the 50 U.S. states as a function of political, legal, and regulatory factors. They find a statistically significant and positive relationship between the growth of entrepreneurial activity—measured by the annual growth rate of sole proprietorships—and states’ scores on an index of economic freedom.

Their results suggest that a state’s economic freedom is an essential factor in the state’s ability to create and attract entrepreneurial activity. The economic freedom index is a composite measure of three areas of state policies: size of government, discriminatory taxation, and labor-market flexibility.3 The table illustrates the positive relationship between the economic freedom score in 1996 and the growth in entrepreneurial activity in the period 1996-2001. The five states with the highest freedom scores experienced, on average, higher growth in the rate of entrepreneurship—measured as the number of nonfarm sole proprietors divided by the population between 25 and 64 years of age—than did the five states with the lowest freedom scores.

These analyses, Kreft and Sobel insist, strongly suggest that political and economic liberties do not work individually to promote economic growth, but rather they exert influence as a complementary group through their incentive effect on entrepreneurial activity.

—Rubén Hernández-Murillo

1United States Small Business Administration, http://www.sba.gov/advo/stats/
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Conventions used in this publication:

1. Shaded areas indicate recessions, as determined by the National Bureau of Economic Research.

2. Percent change refers to simple percent changes. Percent change from year ago refers to the percent change from the same month or quarter during the previous year. Compounded annual rate of change shows what the growth rate would be over an entire year if the same simple percent change continued for four quarters or twelve months. The compounded annual rate of change of $x$ between the previous quarter $t-1$ and the current quarter $t$ is: $\left(\frac{x_t}{x_{t-1}}\right)^4 - 1 \times 100$. For monthly data replace 4 with 12.

3. All data with significant seasonal patterns are adjusted accordingly, unless labeled NSA.

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Real GDP Growth
Compounded annual rates of change

Consumer Price Index
Percent change

Industrial Production
Percent change

Interest Rates
Percent

Change in Nonfarm Payrolls
Thousands

Unemployment Rate
Percent of labor force
### Contribution of Components to Real GDP Growth

Percentage points at compounded annual rates

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### Contributions to Real GDP Growth Rate

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NIPA Chain Price Indexes
Percent change from year ago

Consumer Price Index
Percent change from year ago

Producer Price Index, Finished Goods
Percent change from year ago

Employment Cost Index and Compensation per Hour
Percent change from year ago
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NIPA Chain Price Indexes
Compounded annual rates of change

Gross Domestic Purchases

Compounded annual rates of change

Consumer Price Index

Excl. Food & Energy

CPI (bar)

Compounded annual rates of change

Producer Price Index, Finished Goods

Excl. Food & Energy

PPI (bar)

Compounded annual rates of change

Employment Cost Index

Percentage change from year ago

Benefits

Compensation

Wages and Salaries

Compounded annual rates of change

Oil & Natural Gas Prices: Spot & Futures

Note: Futures prices as of 05/03/2004.

Dollars per barrel

Dollars per million Btu

Spot Oil

Spot Gas

Oil Futures

Gas Futures

Nonfarm

Manufacturing

Unit Labor Cost

Compounded annual rates of change

Compensation per Hour

Compounded annual rates of change

Note: Futures prices as of 05/03/2004.
Employment
Percent change from year ago

Unemployment, Labor Force Participation, and Employment Rates
Percent of labor force

Duration of Unemployment
Percent of labor force
Real Disposable Personal Income
Percent change from year ago, quarterly data

Real Consumption
Percent change from year ago, quarterly data

Retail and Food Services Sales
Percent change from year ago, quarterly average

*Data from Jan. 1992 to the present are on a NAICS basis; data prior to Jan. 1992 are on an SIC basis and are not strictly comparable (see End Note).

Debt Service Payments and Household Debt Outstanding
Percent change from year ago, quarterly data

Percent of disposable personal income
Gross Saving Rates and Balance on Current Account (NIPA)

Percent of GDP

Real Private Fixed Investment
Compounded annual rates of change

Real Equipment & Software Investment
Compounded annual rates of change

Real Nonresidential Fixed Investment
Compounded annual rates of change

Real Residential Fixed Investment
Compounded annual rates of change

Nondefense Capital Goods Orders
Percent change from year ago, excluding aircraft

Housing Starts and New Home Sales
Millions, annual rate

Research Division
Federal Reserve Bank of St. Louis
Government Budgets

**National Income Accounts**

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**Unified Budget**

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National Economic Trends

Trade Balance
Billions of dollars

Current Account Balance
Billions of dollars

Services Trade
Percent change from year ago

Real GDP Growth of Major Trading Partners
Compounded annual rates of change

United Kingdom

Germany

Canada

France

Japan

Mexico

Research Division
Federal Reserve Bank of St. Louis
Output per Hour and Capacity Utilization, Manufacturing

Percent change from year ago

*Data from 1987 to the present are on a NAICS basis; data prior to 1987 are on an SIC basis and are not strictly comparable (see End Note).

Nonfarm Compensation per Hour

Percent change from year ago

Output per Hour, Nonfarm Business and Nonfinancial Corporations

Percent change from year ago

*Data from 1987 to the present are on a NAICS basis; data prior to 1987 are on an SIC basis and are not strictly comparable (see End Note).
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**Updated through 05/04/04**

Research Division
Federal Reserve Bank of St. Louis
## National Economic Trends

**Consumer Price Index**

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<th>Year</th>
<th>Month</th>
<th>Monthly/quarterly</th>
<th>Annual rate</th>
<th>Year ago</th>
<th>Year to date</th>
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**Consumer Price Index less Food and Energy**

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**Producer Price Index Finished Goods**

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<th>Monthly/quarterly</th>
<th>Annual rate</th>
<th>Year ago</th>
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### Updated through 04/22/04

Research Division

Federal Reserve Bank of St. Louis
Notes

Pages 4, 5: Final Sales is gross domestic product (GDP) minus change in private inventories. Advance, Preliminary, and Final GDP Growth Rates are released during the first, second, and third months of the following quarter. Changes result from incorporation of more complete information. Real GDP is measured in 2000 dollars. The ISM (formerly Purchasing Managers’) Index is a weighted average of diffusion indexes for new orders, production, supplier deliveries, inventories, and employment. Aggregate and Average Weekly Hours are paid hours of production and nonsupervisory employees. The Inventory-Sales Ratio uses nominal (current-dollar) inventory and sales data.

Page 6: For information on how to calculate the Contribution of a component to the overall GDP growth rate, see the October 1999 issue of the Survey of Current Business, p. 16. The sign is changed for Imports.

Page 7: Ten-year Treasury Yields are adjusted to constant maturity; three-month yields are secondary market averages. All rates used in the yield curves are adjusted to constant maturity. The 30-year constant maturity series was discontinued by the Treasury Department as of Feb. 18, 2002. Standard and Poor’s 500 Index with Reinvested Dividends shows the total return: capital gains plus dividends.

Pages 8, 9: Oil (West Texas intermediate) and Natural Gas (Henry Hub) spot and futures prices are listed in the Wall Street Journal. Spot prices are monthly averages of daily prices; futures prices are usually taken from the last trading day of the month. Consumer Price Index is for all urban consumers. The Consumption Chain Price Index is the index associated with the personal consumption expenditures component of GDP. The Employment Cost Index (ECI) covers private nonfarm employers. ECI Compensation refers to a fixed sample of jobs, while Compensation per Hour covers all workers in the nonfarm business sector in a given quarter. In both cases, compensation is wages and salaries plus benefits.

Pages 10, 11: Effective with the May 2003 Employment Situation, the establishment survey data for employment, hours, and earnings have been converted from the 1987 SIC system to the 2002 NAICS system. All published NAICS-based labor series have been revised back to at least 1990. For more information see http://www.bls.gov dps/. Nonfarm Payroll Employment is counted in a survey of about 400,000 establishments (Current Employment Survey). It excludes self-employed individuals and workers in private households, but double-counts individuals with more than one job. The Household Survey (Current Population Survey) of about 60,000 households provides estimates of civilian employment, unemployment rate, labor force participation rate, and employment-population ratio. Population is civilian, noninstitutional, 16 years and over. The 90 percent confidence intervals for the unemployment rate (± 0.2 percentage points) and change in household survey employment (± 290,000) measure uncertainty due to sample size. Because the household survey was changed in January 1994, data prior to this date are not strictly comparable. The Bureau of Labor Statistics announced several revisions to the Household Survey on Feb. 7, 2003, with the release of the January 2003 data. For more information, see <www.bls.gov/cps/).

Page 13: The Michigan Consumer Sentiment Index shows changes in a summary measure of consumers’ answers to five questions about their current and expected financial situation, expectations about future economic conditions, and attitudes about making large purchases. The survey is based on a representative sample of U.S. households.

Page 15: Gross Private Saving is the sum of personal saving, undistributed corporate profits with IVA and CCAdj (see notes for pp. 18-19), and private wage accruals less disbursements. Gross Government Saving is net government saving (surplus/deficit) plus consumption of fixed capital. Balance on Current Account (NIPA) is net capital transfer payments to the rest of the world plus net lending or net borrowing (international trade and income flows).

Pages 16, 17: Government Consumption and Investment is current expenditures on goods and services, including capital consumption (depreciation) and gross investment, as reported in the NIPAs. The Unified Federal Budget Surplus/Deficit differs from NIPA Basis in four main ways: (1) NIPA excludes transactions involving existing assets; (2) NIPA outlays exclude government investment and include consumption of government capital, while unified budget outlays do the reverse; (3) NIPA accounts exclude Puerto Rico and U.S. territories; and (4) various timing issues are handled differently. Outlays and Receipts are from the NIPAs, except as noted. Since 1977, the federal Fiscal Year starts on October 1. Excluded agency debt was 0.6 percent of federal debt at the end of fiscal 1997. Federal Debt Held by the Public includes holdings of the Federal Reserve System and excludes holdings of the social security and other federal trust funds. Federal grants in aid to state and local governments appear in both state and local receipts and federal outlays.

Pages 18, 19: The Trade Balance (shown on a balance of payments basis) is the difference between exports and imports of goods (merchandise) and services. It is nearly identical in concept to the Net Exports component of GDP, but differs slightly in accounting details. The Investment Income Balance equals income received from U.S.-owned assets in other countries minus income paid on foreign-owned assets in the U.S. The investment income balance is nearly identical in concept to the difference between gross national product and gross domestic product, but differs in accounting details. The Current Account Balance is the trade balance plus the balance on investment income plus net unilateral transfers to the U.S. from other countries.

Pages 20, 21: Output per Hour (Y/H), Unit Labor Cost (C/Y), and Compensation per Hour (C/H) are indexes which approximately obey the following relationship: % (Y/H) = % (C/Y) = % (C/H) with % (i) meaning percent changes. Unit labor cost is shown on page 9. Real Compensation per Hour uses the CPI to adjust for the effects of inflation. Nonfarm business accounted for about 76 percent of the value of GDP in 1996, while nonfinancial corporations accounted for about 54 percent. Inventory Valuation Adjustments (IVA) remove the effect of changes in the value of existing inventories from corporate profits and proprietors’ income. (This change in value does not correspond to current production and therefore is not part of GDP). Capital Consumption Adjustments (CCAdj) increase profits and proprietors’ income by the difference between estimates of economic depreciation and depreciation allowed by the tax code. Components of national income not shown are rental income of persons and net interest.

NOTE: Most measures of economic activity are now based on the 2002 North American Industry Classification System (NAICS), which replaces the 1987 Standard Industry Classification (SIC) system.

Sources

Bureau of Economic Analysis (BEA), U.S. Dept. of Commerce
National income and product accounts, international trade and investment data (except by country), auto and light truck sales.

Census Bureau, U.S. Dept. of Commerce
Inventory-sales ratios, retail sales, capital goods orders, housing starts, exports and imports by country.

Bureau of Labor Statistics (BLS), U.S. Dept. of Labor
All employment-related data, employment cost index, consumer and producer price indexes, unit labor cost, output per hour, compensation per hour, multifactor productivity.

United States Department of Treasury
Unified budget receipts, outlays, deficit, debt.

Federal Reserve Board
Index of industrial production, treasury yields, exchange rates, capacity utilization, household debt.

The Survey Research Center, The University of Michigan
Consumer sentiment index.

The Conference Board
Help-wanted advertising index.

Organization for Economic Cooperation and Development (OECD)
GDP for major trading partners (not available on FRED).
Dear Customer,

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Sincerely,

Research Division
Federal Reserve Bank of St. Louis

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To receive email notifications when National Economic Trends is updated, users must first register for a user account on the research.stlouisfed.org website. All email accounts are secure, and no information is shared with any third parties. (Go to research.stlouisfed.org/privacy.html for our “Privacy Policy.”) If you already have a user account, please skip over the next section (“How to Create a User Account”) and go directly to Step 4, “Signing up for National Economic Trends Email Notifications.”

• How to Create a User Account

STEP 1

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STEP 2

After Step 1 is complete, the research.stlouisfed.org website will email an account registration notification to the email address that you provided in Step 1. Open this message and please click one of the url addresses provided in the email to proceed to Step 3. (Please note: the url addresses that you receive in your email will be different from the screenshot below.)

Thank you for registering with research.stlouisfed.org, the St. Louis Fed’s economic research web site. In order to activate your account, please visit the following web page on our secure server:

https://research.stlouisfed.org/useraccount/register/step2/

If you experience problems using our secure server, you can use our standard server instead by visiting the following web page:

http://research.stlouisfed.org/useraccount/register/step2/
STEP 3
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and activated a user account at research.stlouisfed.org. Please
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National Economic Trends email notifications.

• Signing up for National Economic Trends
  Email Notifications

STEP 4
Please be sure to log in to your user account before proceeding
to Step 5.

To log in, please visit the research.stlouisfed.org website and
click the “Log In” link, which is on the masthead of each page
on the site.

Users can also log in to their user account by visiting
research.stlouisfed.org/useraccount/login directly.

Please enter your email address and password in the appropriate
fields and click the button labeled “Log in using our secure server.”

STEP 5
Please go to the Publications index
page. This index page can be reached
by clicking the “Publications” link
on the left-hand side of all
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Click on the “Email Notifications”
link that is listed right below the
National Economic Trends header.
STEP 6

You now should have reached the index page that lists every email notification for National Economic Trends. To receive an email notification when a particular National Economic Trends item is updated, please click the “Notify Me of Updates” listed right across from that particular National Economic Trends item. For example, if you want to receive an email notification when a new issue of National Economic Trends is available, please click the first “Notify Me of Updates” link listed on the page.

If you would like to receive additional National Economic Trends email notifications, either hit the “Back” button on your web browser or repeat Step 5 under “Signing up for National Economic Trends Email Notifications.” Then click “Notify Me of Updates” for the additional National Economic Trends item you want to receive through email notification.

Please note that individual pages of National Economic Trends are updated periodically (at various times throughout the month) as new data become available.

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