

Federal investment in small businesses could revive economy after the pandemic

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Recent efforts to support businesses reeling from revenues lost during the pandemic, such as grants and loan programs, have been criticized for favoring larger companies. New research finds that federal agencies get more bang for their buck when they channel grant dollars into smaller startups.

Researchers at Indiana University, Washington State University and the University of Central Florida say their work could provide valuable insights as federal and state governments look for ways to revive the U.S. economy after the pandemic, like the recent Paycheck Protection Program loans.

The study tracked results from about 130 ventures at eight business incubators in the southeastern United States over a four-year period. Small companies receiving their first grant experienced strong revenue growth—an average of 1,000 percent over two years.

By comparison, mid-sized and larger firms in the business incubators reported flat or declining growth trajectories after receiving a grant.

The findings are forthcoming and will appear in a special print issue of *Strategic Entrepreneurship Journal*. The article, "Do Policy Makers Take Grants for Granted? The Efficacy of Public Sponsorship for Innovative Entrepreneurship," was published by the journal online earlier.

"From a public policy perspective, awarding grants to smaller ventures

appears to generate better returns for [economic development](#)," said Alex Kier, assistant professor of entrepreneurship in the WSU Carson College of Business. "We've heard the stories on the news about large, multimillion-dollar organizations that got pretty substantial Paycheck Protection Program loans. Our research indicates that money may have been better spent by spreading out the PPP loans to smaller firms."

Each year, the federal government awards billions of dollars in grants to private companies through entities such as the National Institutes of Health, the National Science Foundation and the Department of Defense. Often, the goal is to stimulate the economy by spurring businesses to create jobs through the development of new products and services.

When [small firms](#) obtain a modest grant, it can increase the company's long-term viability, said Regan Stevenson, assistant professor of management and entrepreneurship and the John and Donna Shoemaker Faculty Fellow in Entrepreneurship at the IU Kelley School of Business. Spreading out available funds in smaller amounts to more early-stage companies may be more effective than providing large grants to more established firms.

"Our data indicates that even micro-grants can produce an inflection point for smaller businesses, rapidly propelling their revenue growth trajectories," Stevenson said. "In addition, we found that when small firms receive their first grant, this also signals to investors that the venture may represent a 'good bet.' As a result, smaller firms immediately become more attractive to investors and secure more external funding."

For larger firms in their incubator sample, the researchers found that "stretching firms" that use resources at hand performed better in the long term than "chasing firms" that seek to acquire and expand resources.

"Stretching firms adopt an innovative and entrepreneurial approach to ensure survival, while chasing firms may seek to develop [grant](#)-writing competency, deterring them from focusing on their core business," said Stevenson, the paper's lead author.

By concentrating grants in a few companies, the federal government might inadvertently squeeze out many worthy competitors, Kier said.

"There's no guarantee the government will pick a winner," he said. "If you think of venture capitalists or angel investors, they are in the [business](#) of investing, and even they sometimes choose unproductive firms. Can you imagine how hard this process is for government agencies?"

More information: Regan Stevenson et al, Do policy makers take grants for granted? The efficacy of public sponsorship for innovative entrepreneurship, *Strategic Entrepreneurship Journal* (2020). [DOI: 10.1002/sej.1376](#)

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