Chapter 12
Low vs. High Income Entrepreneurial Households: Heterogeneous Response to Common Institution Environment in Developing Countries

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ABSTRACT

We explore how income differences influence heterogeneous entrepreneurial responses to the institutional environment in Brazil shapes low-income entrepreneurs’ propensity to exploit the informal rather than the formal economy. Drawing on the Brazilian Global Entrepreneurship Monitor (GEM) data, entrepreneurship discourse and institutional theory, we discuss the influence of inadequate preparedness and barriers to institutional support influencing entrepreneurs’ abilities to engage in productive economic activities. We contribute to the entrepreneurship discourse by suggesting that concepts developed within the context of relatively prosperous settings do not adequately reflect how low-income entrepreneurs respond to institutional settings.

INTRODUCTION

In this chapter, we compare relatively low versus high-income entrepreneurs. Although they all share a common institutional environment, differences between these segments play a role in how entrepreneurs respond to, and operate under, institutional structures. We build on Baumol’s (1990) and North’s (1990) arguments that institutional incentives and structures play a key role in fostering entrepreneurial development. Lawrence et al. (2002: 282) define institutions as “relatively widely diffused practices, technologies, or rules that have become entrenched in the sense that it is costly to choose other practices, DOI: 10.4018/978-1-5225-2673-5.ch012
technologies, or rules”. We postulate that, while the institutional environment may be relatively homoge-
ous within a given country, the degree of poverty (as measured by self-reported household income level) shapes how entrepreneurs engage in business activities, which in turn affect how they respond to, and are supported by, the institutional setting. Our objective is thus to describe how entrepreneurial behavior differs between low-income and high-income entrepreneurs, and how the institutional setting may influence such behavior. We contribute to the entrepreneurship discourse by suggesting that the concepts and theories developed within the context of relatively prosperous settings do not adequately reflect how low-income entrepreneurs will respond to institutional settings, and provide insights on why lower income entrepreneurs often prefer to exploit opportunities within the informal economy.

This chapter supplements the empirical literature on entrepreneurship in weak institutional environ-
ments (Aidis et al., 2008; Johnson et al., 1999, 2000; McMillan and Woodruff, 1999, 2002; Djankov et al., 2005, 2006; Webb et al., 2009), but differs by emphasizing that there are heterogeneous responses to the institutional environment by entrepreneurs, depending on their level of income. It is also a partial response to Bruton et al.’s (2012) call for the “need for an indigenous examination of the firms and managers in institutional settings where informal firms dominate.”

The role of institutions in fostering entrepreneurial development has been widely recognized (Aldrich and Fiol, 1994; Sine et al., 2005). For example, North (1990) argues that economic growth is driven by the incentive structures that encourage individual effort and investment, which in turn is determined by institutions, i.e. society’s ‘rules of the game’, the establishment of which shapes future productive structures (Bygrave and Minniti, 2000). Baumol (1990) argues that, while the supply of entrepreneurial talent is roughly constant, institutions mostly determine entrepreneurial growth that can either encourage productive, unproductive or destructive outcomes. He suggests that productive entrepreneurship will be hindered if the institutional incentives supporting more productive outcomes are weak.

This study considers entrepreneurs in Brazil, a major ‘BRIC’ (Brazil, India, Russia and China) emerging economy (Wilson and Purushothaman, 2003), yet one dealing with social inequality (Griesse, 2006; Hall et al., 2008; 2011). We utilize data collected through the Global Entrepreneurship Monitor (GEM) database to explore the differences between the country’s highest income and lowest income entrepreneurial households. Our objectives are threefold. First, we provide a description of the differences between low and high-income entrepreneurs in Brazil in terms of their socio-demographic and perceptual factors such as entrepreneurial skills and experience, fear of failure, perception of opportuni-
ties and social capital. Second, we describe how these factors influence (i.e., magnitude and direction of affect) an individual’s decision to get involved in a startup business, when analyzing low high-income groups separately. Finally, we explore how these differences lead to heterogeneous responses to common institutional settings.

The remainder of this chapter is structured as follows. In the next section, we provide an overview of the entrepreneurship literature and institutional theory as a theoretical foundation for our empirical analysis. Then we use the entrepreneurship literature to explore the importance of entrepreneurship in developing countries and factors that influence entrepreneurial behavior. We describe our data and method, which is then followed by our comparative analysis of low versus high-income groups and their entrepreneurial behavior. We conclude with discussions on the implications of our work for research and entrepreneurship policy.