

**Comment on Mariassunta Giannetti and  
Andrei Simonov: On the determinants of  
entrepreneurial activity: Social norms, economic  
environment and individual characteristics**

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Quite a large body of academic economic research on self-employment and entrepreneurship has emerged during the last 15 years, perhaps as a consequence of an increased political interest in the subject. Indeed, increased entrepreneurship is seen by many as a potential way of improving an economy's GDP growth and employment growth.

In terms of empirical economic research, the by far most popular research topic has been the determinants of self-employment, i.e. why some individuals are self-employed whereas others are not. In early research, researchers mostly used cross-section data in order to test hypotheses about why someone is self-employed at a given point in time. Owing to endogeneity problems, later research has, to a large extent, made use of longitudinal data. By doing so, it is possible to examine factors that affect the transition into self-employment, using past values of explanatory variables. This approach will mitigate the endogeneity problems (Meyer, 1990).

This branch of research has focussed on a number of topics, for example the effect of personal wealth on the probability of becoming self-employed (e.g. Evans and Leighton, 1989; Evans and Jovanovic, 1989; Holtz-Eakin et al., 1994; Lindh and Ohlsson, 1996; Blanchflower and Oswald, 1998; Johansson, 2000; Taylor, 2001), the effect of taxes (Bruce, 2000; Schuetze, 2000), or the effect of family background (Lentz and Laband, 1990; Fairlie, 1999; Dunn and Holtz-Eakin, 2000; Hout and Rosen, 2000).

### 1. Social norms and self-employment

In the present paper, in addition to reviewing prior research on individual determinants of self-employment, a new direction in the re-

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search on the determinants of self-employment is investigated, namely whether *social norms* affect the probability that an individual becomes self-employed.

Indeed, in economic research, and particularly in theoretical economic research, the idea of social norms is far from new. The central idea in this literature is that individuals interact in other ways than through the price system, or through the exchange of information. Thus, in some way, the idea is that individual behaviour depends on the behaviour of “relevant others”. In empirical economic research, on the other hand, there is not yet very much research on the effects of social norms, probably for the reason that social norms are difficult to quantify. And, importantly, if individual behaviour is dependent on “relevant others”, who are those relevant others? Are they friends, family, or perhaps the inhabitants of the municipality where the individual lives? One example of empirical research on how social norms may affect individual behaviour can be found in Clark (2003). In this paper, the variation in subjective well-being among the unemployed is investigated, and it is hypothesized and found that it is positively related to the unemployment of “relevant others”. In this case, the relevant others are family and the inhabitants of the individual’s region.

It should be noted that in the self-employment literature, the sub-literature on how family background affects the choice to become self-employed lies relatively close to the issues reviewed in the present paper. In that literature, the major finding is that sons and daughters of business owners are much more likely than others to become self-employed themselves. Although this literature has identified some reasons why this is the case, for example that some individuals inherit their parents’ business, it is not unlikely that another explanation may be that having self-employed parents affects the individuals’ preferences in such a way that becoming self-employed becomes more likely.

The basic set-up of the research presented in the present paper is similar to many earlier papers in the self-employment literature. First, the authors estimate an “entry regression”, where the aim is to explain why some individuals become self-employed between time  $t$  and time  $t+1$ , conditional on their not having been self-employed at time  $t$ . Second, they estimate earnings regressions for the self-employed, using the familiar Heckman (1979) two-stage procedure. Third, they estimate a variant of a “survival” function for the self-employed, where the dependent variable takes the value 1 if the individual is self-

employed at time  $t$  and not self-employed at time  $t+1$ , and 0 if the individual is self-employed both at time  $t$  and  $t+1$ . This analysis is similar to the one in Taylor (1999).

The novelty in the research reviewed by Gianetti and Simonov (first and foremost Giannetti and Simonov, 2003) is that they include characteristics of the municipality where the individual lives as an additional regressor in all three analyses described above. The idea is that these municipal characteristics act as measures of social norms in those municipalities, and that these norms affect an individual's entrepreneurial decisions.

A priori, the idea that social norms may affect an individual's decision to become self-employed is probably fundamentally right. However, as Gianetti and Simonov also emphasise in their paper, it is empirically difficult to separate that hypothesis from competing hypotheses. The authors proxy the social norms of the municipality by, among other things, the fraction of entrepreneurs to the population of a municipality, the birth rate and the death rate of firms in the municipality. The authors then show that in municipalities with a high entrepreneurship rate, the probability that an individual starts entrepreneurial activities is significantly higher. This correlation need not be due to the effect of social norms, however. It may well be the case that other municipality characteristics, such as industry structure or geography, affect both the entrepreneurship rate and an individual's decision to become self-employed. For instance, one possibility is that a community is situated by the sea, and is suitable for tourism. Tourism is an industry characterised by small companies, and this may affect both an individual's propensity to become self-employed and the entrepreneurship rate of the municipality.

A possible approach to solve this endogeneity problem is to use instrumental variable techniques. Suitable instruments should, in this case, be correlated with the entrepreneurship rate of the municipality, but uncorrelated with the individual's decision to become an entrepreneur. This approach is, of course, correct if suitable instruments may be found which, in practice, is often difficult. In Gianetti and Simonov (2003), one of the instruments used is the proportion of individuals voting for right-wing parties in the early 1980's. The authors argue that these data, which predate the current analysis, should be exogenous to the entrepreneurship rate of municipalities during the late 1990's. This is an innovative approach, but there is always the risk that political preferences are relatively stable over time within Swedish

communities, and that the proportion of individuals voting for right-wing parties in the early 1980's may still, statistically speaking, be correlated with an individual's propensity to become self-employed in the late 1990's. Nevertheless, given the nature of the problem, Giannetti and Simonov (2003) at least go some way in trying to isolate the effect of social and cultural values on an individual's decision to become self-employed. And, in summary, the authors are probably right in being careful and stating that the fact that individuals who live in municipalities where the entrepreneurship rate is high have a higher propensity to become self-employed may depend on social norms.

## **2. Should self-employment be promoted by public policy?**

The type of microeconomic research presented in Giannetti and Simonov's paper has thus come up with some new interesting insights into why some individuals become self-employed and others not. And thus, from the point of view of a policymaker, some of the results may be used in order to increase the self-employment rate in a society. But what about such a policy, would it be feasible?

In order to answer such a question, it is necessary to study research where the size of the pool of self-employed has been related to important macroeconomic variables, such as GDP growth or employment growth. However, before doing that, one must differentiate between the concepts "self-employed" and "entrepreneur". A self-employed person is simply someone who is working but is not employed by anyone. Self-employment is therefore a more or less statistical concept, which is used in national accounts or labour force surveys. Thus, it is clear that this group of individuals is a very heterogeneous one, which contains everything from the local kiosk owner or baby-sitter to very successful owners of firms, who employ many employees.

The term "entrepreneur", on the other hand, has a long history in economics, and there are many definitions of what entrepreneurship or an entrepreneur is. A modern one is as follows: "Entrepreneurship is the manifest ability and willingness of individuals, on their own, in teams, within and outside existing organisations, to:

- Perceive and create new economic opportunities (new products, new production methods, new organisational schemes and new product-market combinations); and to

- introduce their ideas in the market, in the face of uncertainty and other obstacles, by making decisions on location, form and the use of resources and institutions (Wennekers and Thurik, 1999).

It is clear that if an entrepreneur is someone who performs these tasks, a large number of such people in an economy is no doubt a good thing. The problem is, of course, that if entrepreneurship is defined in this fashion, it is very hard to operationalise and measure empirically. This problem is also clearly manifested in empirical research, where the goal has been to examine the role of entrepreneurship on macroeconomic performance. As no better operationalisation of the number of entrepreneurs in the economy has been available, researchers have used the number of self-employed as a proxy. And the results have generally been disappointing, as it has been difficult to find any positive relationship between the number of self-employed (in a country for instance) and macroeconomic performance. It is perhaps fair to say that the main result stemming from these studies is that the number of self-employed is a bad proxy for entrepreneurial activity. In fact, there is even some evidence in favour of the fact that there may be a negative correlation between the number of self-employed in the economy and macroeconomic performance (Blanchflower, 2000).

Thus, an interesting topic for future research on self-employment is to try to empirically distinguish the entrepreneurs from the self-employed, and examine the factors that affect the prevalence of entrepreneurs in the economy. This will then allow for a more appropriate public policy in the area of entrepreneurship.

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