Self-Employment and Entrepreneurship: Evidence and Implications for the Youth

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The challenge

- MENA is a “young” region: over 50% of population under 25 → huge opportunities and challenges
- Rapid job creation is a pressing need
- If not achieved: growth will be slow, high skilled youth will emigrate, and there will be high youth unemployment and social unrest.
- Private sector is not expanding fast enough
- Key to accelerating job creation in the region: promoting **entrepreneurship and private sector development.**

Entrepreneurship

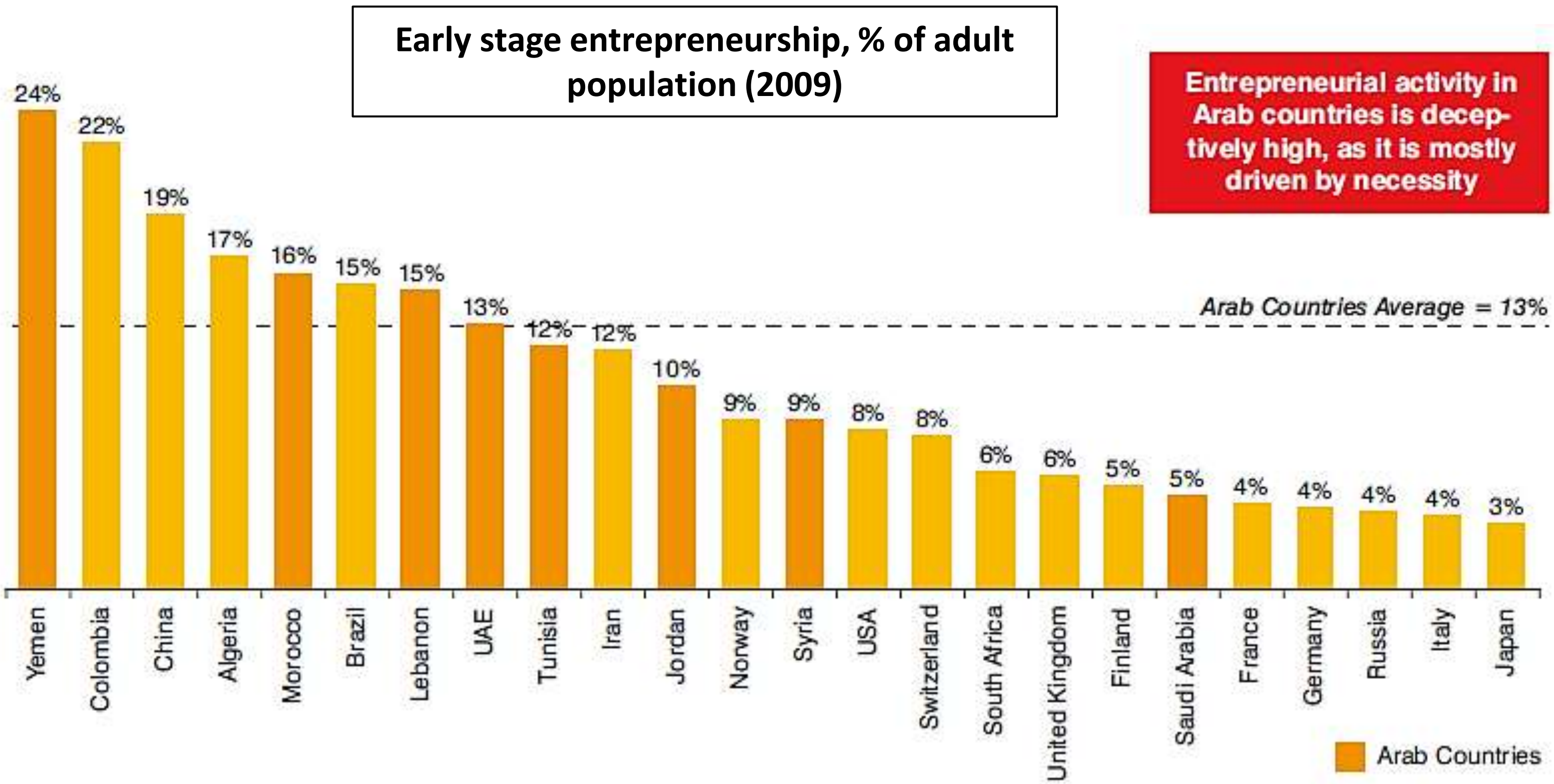
Start-ups not only employ their owners, they also

- create jobs,
- increase innovation,
- raise competition,
- increase efficiency and productivity, and
- provide role models to other young people

Once they mature into small and medium-sized enterprises (SMEs), they become **significant contributors to employment and GDP.**

MENA's entrepreneurial activity today

At first glance, it seems high…



Note: The percentage of the population performing early-stage entrepreneurial activity are those people who are involved in setting up a business or owners-managers of new businesses (less than 42 months).
Source: Global Entrepreneurship Monitor,2009; Booz & Company

… but looks might be deceiving

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- High level of entrepreneurship mainly driven by necessity (not choice)
- More than 80% of entrepreneurs in the MENA region have very small-scale operations (firm values <US$15,000).
- Vulnerable to external shocks
- Most microenterprises do not survive the journey towards sustainable small businesses.
- Why?

Constraints to firm growth

- Access to Capital/Finance
- Managerial Human Capital and Skilled Labor
- Access to Markets
- Regulatory Constraints

Even more pervasive in youth entrepreneurship

What we know, what we don't know…

- Small but growing body of evidence

→ Especially on **access to finance** and **human capital**

- A lot of mixed results
- A lot of heterogeneous effects
- Very little focused on youth

Much more research is needed!

- SME Initiative (IPA)
- Youth Employment Initiative (J-PAL)

Human Capital and Skills

Human Capital and Skills

- Managerial capital improves **productivity** and **financial management** (thus boosting the impact of access to finance)
- Management education and practices are usually worse in developing countries than in developed countries (Bloom and Van Reenen, 2010)
- Business owners may be **missing key skills** and leaving profits on the table.
- However, evidence on potential remedies is **limited and mixed**

Human Capital and Skills

- **Consulting**
  - India (Bloom et al, 2012): management consulting for SMEs increases quality, productivity, output and employment.
  - Mexico (Bruhn, Karlan and Schoar, 2012): consulting services increase sales, profits and productivity but not employment
- **Business training**

Most studies find small but positive impacts of business skills trainings on knowledge and attitudes, but no impact on profits and sales (McKenzie Woodruff, 2012)

  - Peru (Karlan and Valdivia, 2010)
  - Ghana (Karlan, Knight and Udry, 2012).
- **Financial Literacy**
  - Dominican Republic (Drexler, Fischer and Schoar, 2010): no impact on standard, fundamentals-based accounting training; but a simplified, rules-of-thumb based training improves business practices and outcomes. ***Content matters!***

When do training programs work?

Evidence Focused on Youth

Tunisia (Premand et al, 2012):

- Entrepreneurship track in final year of university provides business training and personalized coaching
- Increases self-employment rates one year later (6% for males and 3% for females).
- Channel: fostered business skills, expanded networks, and shaped behavioral skills. (hear more this afternoon!)

Bosnia and Herzegovina (Bruhn and Zia, 2012):

- Financial training increases knowledge for those with low financial literacy
- Improves business performance and sales for those with high initial financial literacy.
- Some improvements in business practices, but no increases in business profits or in business survival rates.

Access to Finance

Access to Finance

Challenges in access to finance for entrepreneurs affect young people **disproportionately**:

- Screening small firms with poor financial infrastructure is hard
  - **Even harder for youth, given their lack of assets, credit history, and information about their productivity**
  - **e.g. Credit scoring** (Schoar and Paravisini, 2013); **personal traits** (de Mel et al 2009)

- Small firms are most sensitive to economic downturns, hurting expected repayment
  - **Youth are even more sensitive due to lack of assets and experience**
  - **e.g. Delaying repayment** (Field et al, 2011)

- Moral hazard: enforcing contracts or seizing assets is difficult
  - **More reluctance to lend to youth, often seen as irresponsible and have no collateral**
  - **e.g. Relationship lending** (Schoar, 2012)

Impact: Cash Grants

Evidence shows **high returns** but **heterogeneous** effects:

- Sri Lanka (de Mel et al 2008)
  - Cash or in-kind grants yield **high returns** (>5%/month)
  - Impacts higher in **male-owned enterprises**
    - Half of female enterprises show *negative* returns
  - Returns are **highest for higher-ability** entrepreneurs and those with fewer other workers in the household

- Ghana: Fafchamps et al (2011)
  - **Huge returns** (15%/month)
  - **Heterogeneous effects** depending on type of grant (cash/in kind) and gender

how high are the returns to capital for young entrepreneurs?

Impact: Microcredit

Randomized evaluations usually find **modest effects** that **vary across groups**:

- Hyderabad, India (Banerjee et al 2010)
  - Households behave differently
    - Entrepreneurs invest in durable assets
    - Non-entrepreneurs spend more on nondurable goods
  - 2nd wave (2013): business profits increase only for businesses above the 85th percentile
- Morocco (Crepon et al 2011)
  - Similar to previous study, decrease in consumption to expand activities only in HHs with a pre-existing business
- Philippines (Karlan and Zinman 2010)
  - Profits increase, but only for men
  - Effects stronger for higher-income entrepreneurs

Not so good at creating entrepreneurs but rather supporting existing businesses (moderately).

Savings

Access to **formal savings, time inconsistencies** (present bias), and **pressure to share** income with peers and family make it hard to save.

- Access to formal **savings accounts** can lead to increased business investment and reduce vulnerability to shocks (Dupas and Robinson 2011 – Kenya Study)
- (Self-)**commitment devices** can increase savings substantially (Ashraf et al. 2005), and can also increase agriculture input use, value of agriculture output and household expenditure (Brune et al. 2011 – Malawi Study)
- **SMS reminders** address limited attention issues (Karlan et al. 2010).

Youth have particularly high rates of future discounting, greater self-control problems, and may be more susceptible to pressure from friends and family to share their money.

A research agenda on youth entrepreneurship

- The important **role of entrepreneurship** for growth and employment creation is largely acknowledged, but we need much more research to figure out **what works to promote it.**
- Existing evidence shows **highly heterogeneous effects**: we need to consider different groups and different contexts. No silver bullet.
- Very **little research focused on youth**:
  - Young entrepreneurs have limited resources, life and work experience, and face **greater barriers** than older entrepreneurs
- Within the youth, different **sub-groups** may have different needs and potential (i.e. gender).
- Human capital: We need to look inside the **black box** of training and get at mechanisms.

Thank you

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