Entrepreneurship and the Informal Economy:
Characterization of Business in Colombia,
an Analysis from the Global Entrepreneurship Monitor

William Niebles Nuñez
Universidad de Sucre, Colombia

Alma Rodero Acosta
Universidad del Atlantico, Colombia

Leonardo Niebles Nuñez
Universidad del Atlántico, Colombia

Ignacio Barrios Parejo
Universidad del Atlántico, Colombia

Hugo G. Hernandez Palma
Universidad del Atlántico, Colombia

Abstract

The existence of informality in the economy has been attributed in large part to unemployment, since this scenario offers income opportunities that are not found in the formal sector; in turn, it has been stated that the reasons for unemployment are rooted in the limitations associated with low levels of education. On the other
hand, globalization has been included among the causes, to the extent that people are not prepared to face this opening; and finally other economic factors have been inserted such as the regulation of the labor market and the size of the public sector, the exchange rate and the economic cycle. For this reason, and with the aim of analyzing the results of a critical documentary review that will provide reflections on the most interesting components, from economic monitoring sources such as the Global Entrepreneurship Monitor, we present the results of this review. The most representative results allow us to analyze the increase in informality and the most notorious effects that it has had on economic systems today.

**Keywords:** Employment, Informality, Development, Business, Competitiveness

### 1 Introduction

It is a fact that informal employment plays a very important role in the economies of countries [1]; informal employment accounts for more than half of non-agricultural employment in most regions of the world: specifically, 82 per cent in South Asia, 66 per cent in sub-Saharan Africa, 65 per cent in East and South-East Asia and 51 per cent in Latin America according to various sources of information [2]. Societies are made up of formal and informal rules, the former correspond to laws and regulations, and the latter are those that are socially shared, created, communicated and applied outside legal channels, and generally arise from the imperfection of formal institutions [3]; the informal economy consists of commercial activities that occur outside formal institutional boundaries but within the limits of informal institutions [4].

### 2 Methodology

In order to achieve the objective that guides the research, a descriptive study is proposed with documentary and longitudinal design in accordance with accepted methodological guidelines for this purpose [5]. In accordance with the above, scientific articles and publications related to the Keywords stated during the period 2010-2018 are reviewed. The population is made up of mainstream serials (journals) that follow up on economic and administrative issues, both in Spanish and English. Global Entrepreneurship Monitor (GEM) figures are also captured. The information collected is organized and tabulated to present the results in an order defined by the researchers’ criteria.

### 3 Results

Authors who have addressed the issue of informality such as Williams, Martínez & Kedir [3] highlight four of the most common generators of institutional imperfections are:
Entrepreneurship and the informal economy …

- The existence of formal institutional gaps, such as a lack of protection of rights, or poor social protection that forces citizens to take their own initiatives to meet their survival needs.
- Inefficiency in formal institutions or misallocation of resources by leaders seeking to favour a specific group of people.
- The existence of institutional uncertainty when technology and socio-cultural changes exceed the capacity of institutions to adapt.
- Institutional weakness and instability, generated from the inability of these to enforce policies and the continuous changes in laws and regulations.

In 1972, the International Labour Organization (ILO) defined the informal sector based on seven factors: ease of entry, reliance on native resources, family enterprises, small-scale operations, technology in intensive and adapted labour, skills acquired outside the formal school system, and unregulated and competitive markets [7].

On the other hand, the International Conference of Labour Statisticians (ICLS) defined the sector based on the economic activities that take place in domestic or unincorporated enterprises, associated with the provision of goods and services for remuneration, but developed with little or no compliance with formal aspects, this definition includes all private, unincorporated enterprises that do not register their salaried employees, or below a certain size threshold, that produce at least some of their goods and services for sale or barter [6]. Some of the main factors that impact on participation in the informal economy can be categorized into two categories: exclusion or choice, the most common of which are presented in the following table.

Table 1. Factors determining participation in the informal economy
(De Beer, Fu, & Wunsch, 2013).

<table>
<thead>
<tr>
<th>By exclusion</th>
<th>By choice</th>
</tr>
</thead>
<tbody>
<tr>
<td>The limited capacity of the formal economy to absorb labour supply.</td>
<td>The existence of demand for low-cost goods and services.</td>
</tr>
<tr>
<td>Economic and poverty difficulties.</td>
<td>Few barriers to entry into the informal economy.</td>
</tr>
<tr>
<td>The existence of entry barriers to the formal economy.</td>
<td>The desire to generate unregulated income.</td>
</tr>
<tr>
<td>Insufficient provision of education, training and infrastructure of formal institutions.</td>
<td>Dissatisfaction with formal employment.</td>
</tr>
<tr>
<td>Negative impact of globalization on less skilled workers.</td>
<td>Desire for independence and control.</td>
</tr>
<tr>
<td>Difficulties in the formalization of business by undocumented persons.</td>
<td>Observance of a competitive advantage in commercialization with prices below the formal market.</td>
</tr>
<tr>
<td>Inability to secure formal employment</td>
<td>The informal economy seen as the first stage in the search for formal businesses.</td>
</tr>
</tbody>
</table>
On the other hand [7], highlights the nature and composition of the informal economy in four schools of thought:

- Dualist school: includes activities that are marginal, not related to the formal sector and that generate income for people on low incomes and offer a framework of security for future times of crisis. Its members support their participation by arguing that informal businesses are excluded from the imbalances generated by the differences between people's skills and the opportunities offered by modern economies.

- Structuralist school: it perceives this economy as a group of economic units and subordinate workers, working with low cost inputs and labour, in order to increase its degree of competitiveness against large capitalist companies. Structuralists argue that the nature of capitalist growth and/or capitalism drives informality.

- Legalist school: formed by microentrepreneurs, who decide to work in the informal sector in order to avoid the costs, time and effort required by formality. Supporters of this school argue that a hostile legal system leads independent workers to operate informally under their own informal and extra-judicial rules.

- Voluntary school: it also includes businessmen who enter the informal sector deliberately in order to avoid regulation and taxes, but do so without blaming the cumbersome registration procedures. The members of this school argue that informal business arises from the evaluation of the cost-benefit ratio of informality versus formality.

On the other hand, researchers Galvis [8] and Jiménez [9] focus on two approaches to explaining labour informality: the structuralist and the institutionalist. The first category results from the dualist theory that contemplates the existence of a modern and a traditional economic sector; it brings together large companies with intensive production techniques, high levels of productivity and a supply of high quality jobs; while the second category brings together small productive units, motivated by subsistence, and therefore their job offer is of low quality, have production techniques based on the use of labor, and low productivity [9]. This approach establishes survival as the main motivator, finding informality as an alternative to overcome situations where opportunities to obtain good jobs are scarce, generated by the existence of segmented labor markets in a country [9]. The following factors have been identified as promoting this trend, from the point of view of the demand and supply of a particular economy, and are shown in Table 2.
Table 2. Factors associated with informality in the structural approach (Galvis, 2012)

<table>
<thead>
<tr>
<th><strong>Demand</strong></th>
<th><strong>Supply</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Poor structural development of the economy.</td>
<td>The demographic transition, when the mortality rate has already decreased but the birth rate is still high.</td>
</tr>
<tr>
<td>Use of capital-intensive technologies.</td>
<td>Rural-urban migratory flows.</td>
</tr>
<tr>
<td>The policy of downsizing the state, which ends formal jobs.</td>
<td>Greater involvement of family members other than the head of household, especially women.</td>
</tr>
<tr>
<td>Low levels of investment.</td>
<td></td>
</tr>
</tbody>
</table>

As we have seen, the informal economy depends directly on entrepreneurship, which has three basic components: innovation, risk and proactivity [10]; the way in which these are exploited depends on the skills and motivations of the entrepreneur. The GEM has defined several phases of entrepreneurship, initially starting with potential entrepreneurs, such as those who see opportunities in their area and believe they have the capacity to start a business, in which beliefs greatly influence them in order not to be discouraged in the face of the possibility of failure. Second, there must be an intention to start a business, followed by the birth of the activity, and continuing with the establishment of the business and the possible closure, considered by entrepreneurs who see an opportunity to finish the current activity and start a new one [11].

On the other hand, Zahra & Wright [12] identified five pillars that define the social role of the entrepreneur:

- Entrepreneurship actors: there are a variety of actors involved in an entrepreneurial environment, not just the individual entrepreneur, understanding institutions and other companies, both new and established, as influential in the birth and growth of entrepreneurship. The diversity of these groups and their multiple needs affect the behaviour of these new companies and also shape the evolution of their environments.
- Development of entrepreneurship: a large part of entrepreneurship is the result of a need for employment, so this aspect refers to the activities of entrepreneurs, which may be productive, unproductive or dysfunctional, forcing them to analyze the way in which activities should be developed and what actions are needed to make them happen.
- The form of entrepreneurship: as noted above, the development of a new activity can be carried out formally and informally, so the entrepreneur must
consider the legality of the enterprise and otherwise consider its consequences.

- The impact of entrepreneurship: the entrepreneurial spirit affects communities, societies and humanity, so the work of entrepreneurs must go beyond the generation of wealth and address issues related to food and water scarcity, environmental pollution and degradation and sustainability.
- Measuring the impact of the initiative: this refers to measuring growth and financial performance, as well as social impact measures such as community development, happiness and social cohesion.

Entrepreneurship is a complex concept that encompasses the creation of ideas, companies and patents, as well as the thought process behind these creations [13]. Dana [14] recognizes the entrepreneur as a person absorbing the uncertainty caused by changing conditions, taking advantage of them in such a way that they contribute to society; on the other hand, Kuratko [2] describes entrepreneurs as people who recognize opportunities where others see chaos, contradiction and confusion, acting as aggressive catalysts for change within the market. It is for this reason that Solesvik [15], based on his own study, identified the most outstanding competencies of people in their actions as entrepreneurs:

- Identifying opportunities: the ability to see opportunities in a business environment.
- Relationship: associated with building networks, building trust with suppliers and customers.
- Decision-making: this is related to the development of ideas, decision-making and risk.
- Commitment: skills to boost business and achieve objectives
- Organizational: associated with the company's performance such as managerial, human resource management and financial management competencies.

Having reviewed the theory of the types of entrepreneurship and the typical skills of entrepreneurs, it is important to highlight some of the motivations that have resulted from the development of various research projects on this activity [16]: personal aspirations: related to motivations of security, profit, social service, independence and the interest in carrying out management activities; motivations of a material nature: associated with the accumulation of capital or the development of social relations; negative motivations: resulting from work experiences that may have generated job frustration and obtaining specific knowledge about the market, the product and others related to the entrepreneurial activity. Finally, the GEM for 2016 [17] has reported in recent years on the evolution of entrepreneurship in Colombia, citing the figures shown in figure 1.
Entrepreneurship and the informal economy ...

Fig. 1: Characterization of entrepreneurship in Colombia (GEM, 2016)

The above figures suggest that in Colombia informality has become apparent and silent. Thus, the formalities processes must be strengthened in order to provide the entrepreneur with guarantees and confidence [18], so that aspects such as innovation, training and the insertion of technologies are taken into account for their economic growth and development. Encouraging these small initiatives on a massive and permanent basis can certainly lead to a new economic landscape [19-20].

4 Conclusion

When researching the roots of informality, it is common to find components such as unemployment, public policies and education. In Colombia, the entrepreneurial process has grown positively, however, the figures provided by the GEM show that there is still a very high degree of informality. Although the research consulted indicates that this situation may be due to factors such as exclusion or will, depending on each case, it is undeniable that support from the State is indispensable with good policies to encourage formality and thus forge a more stable scenario where supply and demand are relatively balanced. Thus, aspects such as the insertion of technologies, economic training and innovation should be considered for the promotion of organized entrepreneurship in the country.

References

[1] D. Cardona, A. M. Rada and H. G. H. Palma, Creación de empresa como pilar para el desarrollo social e integral de la región caribe: Apuntes críticos, Saber,
Ciencia y Libertad, 12 (2017), no. 1, 15.


2659


Received: June 19, 2018; Published: July 19, 2018