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Article

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THE ROLE OF START-UP INCENTIVES ON ENTREPRENEURSHIP DYNAMICS IN A POST-CRISIS ERA: EVIDENCE FROM EUROPEAN COUNTRIES

ANA MILLÁN¹, JOSÉ MARÍA MILLÁN² AND CONCEPCIÓN ROMÁN³

Introduction

Almost one decade after the financial and economic crisis started, the outlook for the global economy is still uncertain. In the European context, persistent turbulences such as systemic instability in banking systems coexist with new threats like the impact of the Brexit vote. As a result, the ability of the EU to stimulate growth and create jobs is still in doubt. This is especially true of some European countries that have suffered substantial increases in unemployment rates since 2008. Indeed, the seasonally-adjusted unemployment rate in May 2016 was 8.6 percent for the EU-28, while it was as high as 10.1 percent for the Euro Area (EA-18). Among the EU member states, the highest unemployment rates were recorded in Greece (24.1 percent in March 2016) and Spain (19.8 percent) (Eurostat 2016). The challenge is therefore not just to strengthen the economic resurgence, but also to ensure that this recovery is accompanied by employment growth.

In this sense, there is almost a consensus among academics and policymakers that entrepreneurship is a major driver of economic growth, job creation, and competitiveness in global markets (e.g., Carree and Thurik 2008; Parker 2009; European Commission 2010, 2013, 2015). Precisely within the framework of the *Europe 2020 Strategy*, Europe is diagnosed as suffering from a *lack of entrepreneurs*, which needs to be corrected in

order to trigger a return to higher growth and levels of employment (European Commission 2013).

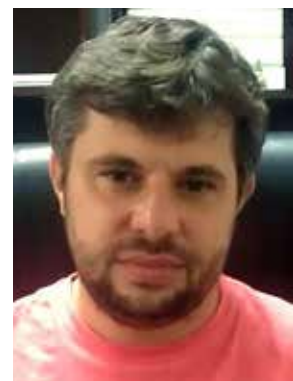
However, the most effective path towards creating a favourable environment to support entrepreneurship remains unclear, as this seems to depend heavily on market conditions and their actual regulation (Millán et al. 2013, 2015a; Millán, Congregado and Román 2012; Román, Congregado and Millán 2011, 2013; Román et al. 2016; Sanchis-Llopis et al. 2015). Indeed, despite many empirical evaluation studies, there is no clear-cut evidence on the effectiveness of some of the most important Labour Market Policy measures (henceforth LMP measures) including those incentives specifically designed to stimulate entrepreneurship, i.e., start-up incentives (Altavilla and Caroleo 2013).

This absence of sharply outlined results regarding the role of start-up incentives may occur because self-employment (the most common proxy for entrepreneurship in empirical studies) is a heterogeneous group, wherein only a minority are entrepreneurs in the sense of creating firms that generate both innovation and wealth (Blanchflower 2004; Carree et al. 2007; Shane 2009) and/or hire other workers – i.e., enter employer-ship (Millán et al. 2015b; Cowling, Mitchell and Taylor 2004). In other words, (i) the effect of start-up incentives on different types of self-employment may differ; and (ii) more self-employment is not necessarily better.

The distinction between self-employed individuals with and without employees assumes particular importance at a time like this. This distinction separates self-employment into those employers who hire external labour (and contribute to the job-generation process), and those who work on their own (own-account workers), who can be considered as proxies for *true* entrepreneurs and less entrepreneurial forms of self-employment (such as *last resort*⁴ or *dependent*⁵ self-employed), respectively

⁴ Self-employment as a last resort refers to those entering self-employment due to a lack of paid-employment opportunities (Alba-Ramírez 1994; Blume et al. 2009; Rissman 2003).

⁵ Dependent self-employed workers are self-employed without employees whose conditions of work are nonetheless similar to those of employees, in the sense that they work mainly or exclusively for a specific client-firm with limited autonomy and are often closely integrated into its organisational structure (OECD 2014). As a result, this type of contract represents another flexible and often low-cost alternative to regular, open-ended employment contracts (Parker 2010; OECD 2014).



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(Earle and Sakova 2000; Kuhn 2000; Román, Congregado and Millán 2011, 2013).

Hence, a comprehensive strategy to promote job creation and sustained economic growth in a *post-crisis era* may involve reconsidering some aspects of entrepreneurship, such as its heterogeneous character, and the different effects that LMP measures (and the economic situation) might cause on its different types.

This article's main aim is to shed light on precisely this issue. To this end, we begin by describing the evolution in European macro figures on (i) unemployment, (ii) expenditure on LMP measures, and (iii) self-employment for the period 2008–14. Secondly, we revise existing literature on the role of start-up incentives on self-employment dynamics and recall the main results of three of our previous studies (Millán, Congregado and Román 2012; Román, Congregado and Millán 2011, 2013) on the effects of start-up incentives and economic conditions on transitions from unemployment and paid employment to self-employment, as well as on self-employment survival. Finally, the last section of this article presents some concluding remarks.

Unemployment, labour market policy and self-employment in the EU-15

Unemployment in the European Union has evolved along different lines for the various member states since the beginning of the financial and economic crisis. Figure 1 shows unemployment rates for the 15 member states between 2008 and 2014.

During this period, the proportion of unemployed people increased in all countries, with the exception of Germany. The magnitude of the rise, however, varied markedly between member states. For example, the un-

Figure 1

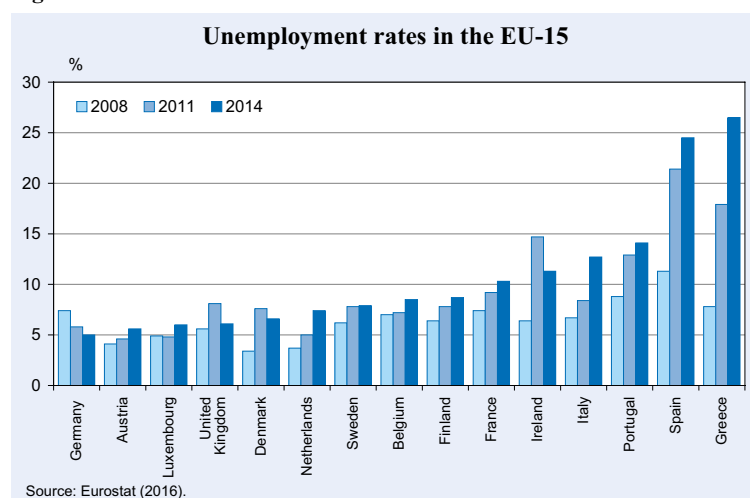
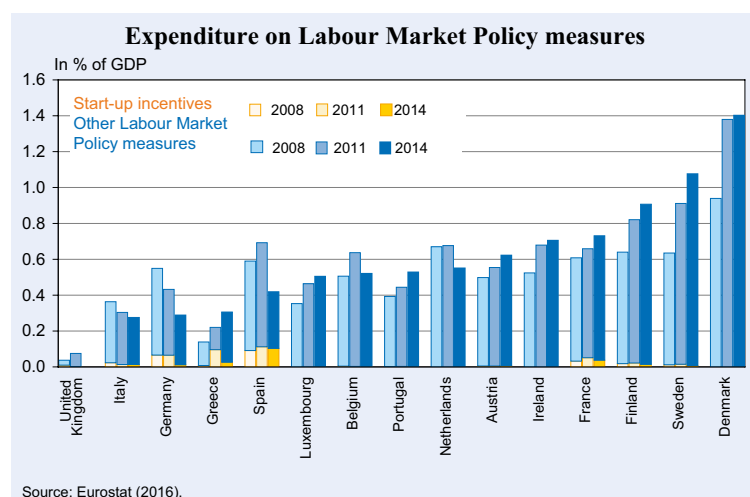


Figure 2



employment rate growth was particularly high in Greece and Spain where the share increased by 18.7 and 13.2 points, respectively. For the remaining member states, the rise in the unemployment rate was below six points.

In parallel, government actions to help and support unemployed people and other disadvantaged groups in the transition from unemployment or inactivity to work also differed significantly between countries in the period under consideration. Figure 2 shows national expenditure on LMP measures as a percentage of GDP between 2008 and 2014.⁶ LMP measures cover interventions that provide temporary support for groups that are disadvantaged in the labour market and which aim to activate the unemployed, helping people move from involuntary

⁶ Due to missing data, 2014 figures for Spain and Ireland refer to 2013 and 2011 figures for Greece and UK refer to 2010.

Figure 3

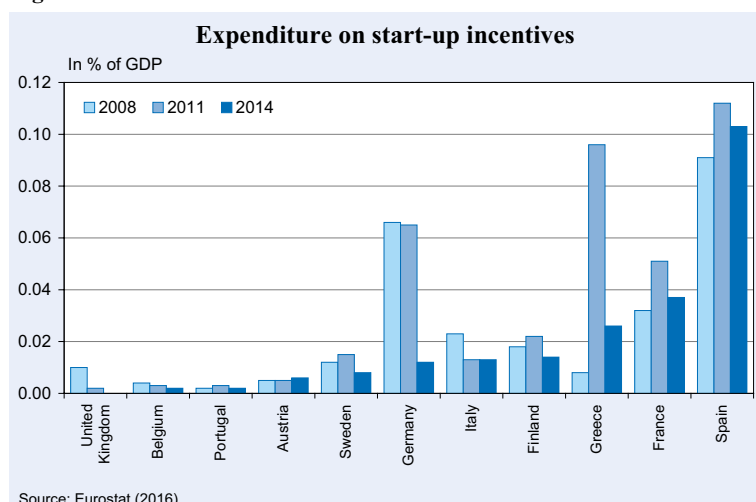
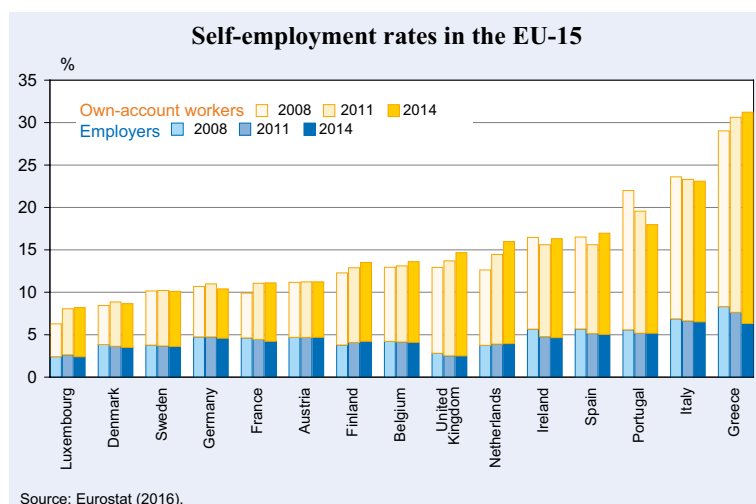


Figure 4



inactivity into employment, or maintaining the jobs of persons threatened by unemployment. The expenditure on LMP measures can be split into five categories: (1) training, (2) employment incentives, (3) supported employment and rehabilitation, (4) direct job creation and (5) start-up incentives.⁷

Focusing on 2014 figures, Italy, Germany and Greece had the lowest expenditure on LMP measures, while Denmark, Sweden and Finland topped the list for LMP measure spending. This expenditure increased between 2008 and 2014 in all countries apart from Italy, Germany, Spain and the Netherlands. However, the level and evolution in this spending were not the only factors that differed between countries.

⁷ A detailed description of these categories can be found in Eurostat (2013).

The relative emphasis on different types of measures also varied considerably between member states. In particular, Figure 2 shows the relative importance of expenditure on start-up incentives – a measure that includes programmes that promote entrepreneurship by encouraging the unemployed and target groups to start their own business or to become self-employed – over total spending. The highest proportions of total spending dedicated to start-up incentives in 2014 correspond to Spain (24.5 percent), Greece (8.5 percent) and France (five percent). This proportion is lower than one percent in Belgium, Portugal, Austria and Sweden. Finally, Luxembourg, Netherlands, Ireland and Denmark did not spend resources on such measures. Figure 3 shows the evolution of expenditure on start-up incentives as a percentage of GDP during the period under consideration for countries with positive spending on this measure.⁸

Figures 2 and 3 show that, despite the prominent role of entrepreneurship as a job creation enhancer, the measure directly related to its promotion is not at the heart of

the European LMP. Thus, the highest expenditure on start-up incentives for the whole period is below 0.12 percent of GDP, while the average is just about 0.02 percent of GDP. Figure 3 also highlights that there have been pronounced differences in the use of these incentives in the EU-15 since the global crisis started.

In line with the above findings, it is not surprising that self-employment rates differ substantially across countries. Figure 4 shows the evolving rates of self-employment during the period 2008–2014, distinguishing between self-employed with employees – employers – and self-employed without employees – own account workers.

⁸ Due to missing data, 2014 figures for Spain and Ireland refer to 2013 and 2011 figures for Greece and UK refer to 2010.

Self-employment rate levels ranged from 6.28 percent in Luxembourg in 2008 to 31.22 percent in Greece in 2014. During the period under consideration, the proportion of self-employed people increased in all countries, apart from Germany, Ireland, Italy, Portugal and Sweden. This aggregated pattern corresponds with the evolution of the share of own-account workers – that increased in all member states, with the exception of Germany, Italy, Austria and Portugal. Inversely, the share of employers diminished in almost all countries. An increase in this rate of no greater than half of a point was only seen in the Netherlands, Austria and Finland.

In sum, European macro data for the period 2008–14 show that unemployment rates, expenditure on LMP measures in general – and on start-up incentives in particular – and self-employment rates have evolved in varied ways in different countries. To illustrate the difficulty of drawing conclusions about the relationship between start-up incentives and self-employment rates using descriptive data, let us compare the situation of two pairs of countries. On the one hand, we observe that countries like Germany and Spain – that have made major efforts to promote self-employment – show levels and evolutions in self-employment rates that are rather different. On the other hand, countries with low levels of expenditure on start-up incentives as the United Kingdom and Portugal also present different – and even opposing – patterns of self-employment rate dynamics. Individual factors, as well as other institutional variables, may shape this relationship. Therefore, to be able to understand the impact of start-up incentives on self-employment rates and its composition, it is necessary to use conditional analyses, like those mentioned in the next section.

Existing literature on the relationship between start-up incentives and self-employment

One possible impediment to becoming an entrepreneur is simply a lack of capital. An important stream of literature has emphasised the role of liquidity constraints on the decision to start a new business (Blanchflower and Oswald 1998; Cabral and Mata 2003; Evans and Jovanovic 1989; Holtz-Eakin, Joulfaian and Rosen 1994; Hurst and Lusardi 2004; Kan and Tsai 2006; Lindh and Ohlsson 1996; Taylor 2001). In this sense, there is evidence of discrimination in the credit market against certain socio-economic groups, such as minorities, women and the unemployed (Blanchflower, Levine and Zimmerman 2003; Blanchflower 2009; Cavalluzzo,

Cavalluzzo and Wolken 2002). As a result of such discrimination, public self-employment support has been introduced as an increasingly important policy measure in many countries. Despite variations across countries in the number of participants, the eligibility criteria, and the level of expenditure, these schemes share a common feature; i.e., they offer unemployed individuals and other disadvantaged groups economic incentives for the start-up phase of their self-employment activity.

In this sense, because policymakers have subordinated start-up programmes to the objectives of LMP (Baumgartner and Caliendo 2008), the effectiveness of these incentives has been tested as employment policy instead of entrepreneurship policy. As a result, the contribution to some relevant entrepreneurship policy objectives, such as economic growth or innovation, has been overlooked. In addition, it has been argued that this is bad public policy in the sense that encouraging more people to start businesses will not enhance economic growth or create many jobs because start-ups are generally not the source of economic vitality or job creation (Congregado, Golpe and Carmona 2010, Shane 2009).

Thus, taking into account the heterogeneous character of self-employment becomes crucial to better understanding the contribution of start-up incentives to job creation, growth and innovation processes. Following on from this, and to conclude this section, we recall the main results of three of our previous studies (Millán, Congregado and Román 2012; Román, Congregado and Millán 2011, 2013) on the effects of start-up incentives and economic conditions on self-employment dynamics and its composition, where this heterogeneity is considered. Using microdata from the European Community Household Panel (henceforth ECHP)⁹ these analyses focus not only on the effect of individual characteristics, but also on specific regional factors through the introduction of measures of the European economic conditions and regulatory environments. As far as the role of start-up incentives is concerned, these key results can be summarised as follows.

Firstly, Román, Congregado and Millán (2011) showed that public expenditure on start-up incentives has positive effects on transitions from paid employment to

⁹ The ECHP is a panel of households in the EU-15 (about 54,000 individuals), covering the period 1994–2001. Every year, all members of the selected households in each country are interviewed on issues related to demographics, the labour market, incomes and living conditions. The same questionnaire is used for all countries, which makes the information directly comparable. The ECHP data are used with the permission of Eurostat (contract ECHP/2006/09, held with the Universidad de Huelva).

self-employment, which seems to support the positive effect of these incentives for overcoming obstacles associated with self-employment status. However, this effect is stronger for individuals entering *dependent* self-employment than for those entering independent self-employment.¹⁰ Hence, further research into the contribution to economic growth and to job creation processes of both groups is required to design appropriate entrepreneurship policy.

Secondly, Román, Congregado and Millán (2013) analysed transitions from unemployment and demonstrated that the expenditure on start-up subsidies increases the probabilities of entering own-account self-employment, whereas it does not seem to have any effect on employership. However, the authors also found evidence of a differentiated effect of these incentives in terms of the unemployment rate for transitions to self-employment with and without employees. In this sense, periods with higher unemployment rates are precisely those in which the positive effect of start-up incentives for individuals entering own-account work is weaker. In addition, and even more interestingly, the incidence of these incentives for those entering employership becomes negative in recession periods, precisely when their use is more intensive. Analogously, another interesting result refers to the differentiated effects of the expenditure on start-up incentives for individuals receiving and not receiving unemployment benefits, detected for transitions to own-account self-employment. Thus, the positive effect of these subsidies is also stronger for those unemployed not receiving unemployment benefits, that is, the natural candidates to accept any available form of employment in such circumstances, including *last resort* or *dependent* forms of self-employment. Therefore, to evaluate the effectiveness of these incentives, it becomes crucial to first define their policy objectives. If, as part of LMP, start-up incentives are intended to improve the chances of people moving back into work, they can be considered adequate instruments in the light of our results. Nevertheless, if considered as an entrepreneurship policy, these incentives aim not only to enhance self-employment, but also to favour those forms of self-employment that further contribute to economic growth and job-creation processes. The effective design of these types of incentives therefore becomes crucial.

Thirdly, Millán, Congregado and Román (2012) showed that expenditure on start-up subsidies decreases the risk of exiting self-employment, specifically for the group of individuals entering self-employment from unemployment – i.e., the target group for these incentives. These incentives may therefore be seen as a route not only to increase entry into self-employment, but also to equalise the survival chances of individuals entering self-employment from unemployment and those entering with a different starting status.

Conclusions

As several European governments have shown a renewed interest in the development and implementation of new start-up programmes in recent years, the appropriateness of these policies lies at the heart of present policy debate. Nevertheless, because the self-employed can be considered a heterogeneous group, among which only a minority of self-employed people contribute to job creation, economic growth and innovation, more self-employment is not necessarily better. Understanding how these subsidies and other context-related factors may affect the relative weight of *true* entrepreneurs over other categories within self-employment could be crucial to improve the effectiveness of measures aimed to stimulate self-employment among the unemployed.

To shed light on precisely this issue, in this article, we revise existing literature on the role of start-up incentives on self-employment dynamics and recall the main results of three of our previous studies (Millán, Congregado and Román 2012; Román, Congregado and Millán 2011, 2013) on the effects of start-up incentives. Our empirical results show how these incentives might be distorting the occupational choice against *true* entrepreneurs in favour of certain forms of self-employment – such as *last resort* or *dependent employment* and, therefore, stress the risk of using a unique recipe from a public policy perspective when defining instruments for self-employment promotion. Furthermore, these effects appear to be shaped by the aggregated economic situation and the receipt of unemployment benefits. Thus, highly impoverished groups such as unemployed individuals in periods of higher unemployment or those who are not receiving benefits seem to enjoy higher own-account work chances in the presence of start-up incentives, whereas their employership chances are either weakly increased (when not receiving benefits) or even reduced (during recessions). On a broad policy level, therefore, taking into account macroeconomic

¹⁰ *Independent* self-employment refers to entrepreneurship spurred by a business profit opportunity, with a cessation of formal and informal labour relationships with the previous employer (and that can be considered true entrepreneurs). By contrast, *dependent* self-employment refers to self-employed workers who are employed with the same tasks by the same employer for whom they previously worked as employees.

conditions and the personal circumstances of the potential beneficiaries seems highly relevant when designing these incentives.

Nevertheless, prior to evaluating the effectiveness of policy intervention in this area, a much deeper reflection on policy objectives and target groups is required, focusing on the key question of whether start-up incentives are considered an entrepreneurship policy or, on the contrary, an instrument within LMP. If, as part of LMP, start-up incentives are intended to improve the chances of people moving back into work, they can be considered adequate instruments in periods of moderate unemployment, in the light of our results. On the contrary, if, as part of the entrepreneurship policy, these incentives are considered as an instrument to combat economic and job crises, their contribution is dubious at the very least. These results are in line with previous research that questions the appropriateness of incentives that encourage unemployed people to become self-employed, and stresses the need for highly selective policy incentives that focus more on innovative and high-growth entrepreneurship (Congregado, Golpe and Carmona 2010; Santarelli and Vivarelli 2007; Thurik et al. 2008).

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