



Non-farm entrepreneurship in rural sub-Saharan Africa: New empirical evidence



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ABSTRACT

We report on the prevalence and patterns of non-farm enterprises in six sub-Saharan African countries, and study their performance in terms of labor productivity, survival and exit, using the World Bank's Living Standards Measurement Study - Integrated Surveys on Agriculture (LSMS-ISA). Rural households operate enterprises due to both push and pull factors and tend to do so predominantly in easy-to-enter activities, such as sales and trade, rather than in activities that require higher starting costs, such as transport services, or educational investment, such as professional services. Labor productivity differs widely: rural and female-headed enterprises, those located further away from population centers, and businesses that operate intermittently have lower levels of labor productivity compared to urban and male-owned enterprises, or enterprises that operate throughout the year. Finally, rural enterprises exit the market primarily due to a lack of profitability or finance, and due to idiosyncratic shocks.

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1. Introduction

A significant number of rural households in sub-Saharan Africa do not limit labor allocation to agriculture, but also operate and work in non-farm enterprises (Reardon et al., 2006).¹ Over time the contribution of these enterprises to household incomes and employment has increased rather than decreased, as some development economists in the 1960s and 70s expected (Lanjouw and

Lanjouw, 2001; Start, 2001; Haggbjale et al., 2010). This contribution is unlikely to diminish in the future given that rural businesses will be needed to support the job creation for the roughly 170 million new job seekers entering Africa's labor market between 2010 and 2020 (Fox and Pimhidzai, 2013). In this regard it is useful to have an up-to-date and accurate profile of the prevalence, patterns and performance of rural enterprises. So far most existing empirical work on African entrepreneurship is based on one-period, single-country and rather limited survey data. And although comprehensive research has been done to study the income diversification of rural households and the determinants thereof (see Davis et al., 2010, 2014), systematic knowledge on the performance of rural enterprises is virtually non-existent.

Hence, the contribution of this paper is twofold. First, it provides up-to-date and comparative evidence on the prevalence and patterns of rural enterprises. Second, it provides an empirical analysis of their performance, as well as a set of descriptive statistics on their survival and exit. We use the Living Standards Measurement Study - Integrated Surveys in Agriculture (LSMS-ISA) data set, a nationally representative data collection covering six

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¹ In this paper non-farm entrepreneurship is described as any kind of business activity in the non-farm economy that is undertaken by the active rural population. Non-farm enterprises are business ventures started and managed by households outside of agriculture. They typically include many heterogeneous activities such as food-processing, trade and sales, services, as well as construction and transportation activities (Wiggins and Hazell, 2011). Although referred to as non-farm, many of these enterprises are linked to agriculture and can be located on a farm, for example food processing or veterinary services (Rijkers and Costa, 2012).

countries over the period 2005 to 2013, namely Ethiopia, Malawi, Niger, Nigeria, Tanzania and Uganda. It is the first time, to the best of our knowledge, that this data set is used to study Africa's rural enterprises.

Our main results are as follows. First, we confirm the prevalence of rural entrepreneurship as established in the existing literature. To be specific, we find that almost 42 percent of rural households operate an enterprise. Relevant determinants of this decision are household size, the experience of shocks, access to credit and markets, household wealth and various individual characteristics of the household head. Most households operate businesses in easier-to-enter activities, such as sales and trade, but fewer households in activities that require higher starting costs or educational investment. Second, rural and female-headed enterprises, those located further away from population centers, and businesses that operate intermittently, report lower levels of labor productivity than urban and male-owned enterprises, or enterprises that operate throughout the year. Education or the experience of a shock are further relevant factors affecting labor productivity. Third, we find that enterprises exit the market primarily due to a lack of profitability or finance, and due to idiosyncratic shocks.

The paper is structured as follows. In Section 2 we summarize the current state of knowledge on non-farm entrepreneurship in rural Africa. In Section 3 we describe the LSMS-ISA data set and its shortcomings, and present descriptive statistics on the prevalence and patterns of rural enterprises, followed by an analysis of the decision to operate a business in Section 4. In Section 5 we report our empirical findings on the performance of these enterprises, as well as descriptive statistics on survival and exit. The final section concludes.

2. Literature review

In the year 2000 Wiggins (2000) lamented that 'little is known' about Africa's rural non-farm economy, beyond an 'embryonic set of ideas'. Since then the embryonic set of ideas has been elaborated in more detail by scholars, particularly with respect to the decision of entering entrepreneurship, and the contribution of non-farm enterprises to household income and employment. The performance, survival and exit of these enterprises, however, have largely been neglected.

2.1. The decision to operate a business

The literature on the decision to enter entrepreneurship has identified both push (necessity) and pull (opportunity) factors (Herrington and Kelly, 2012). Pull factors include opportunities to earn an income during the lean season, while push factors include low incomes and negative shocks (Barrett et al., 2001). The households' desire to maintain consumption in the face of risks and incomplete insurance and credit markets can motivate them to reduce their exposure to shocks by operating such an enterprise (Janvry and Sadoulet, 2006; Dercon, 2009).

This enterprise type, generally 'family firms', reflects the household's exposure to risk. Family ties can provide informal insurance to households given limited social security and a high-risk environment (Bridges et al., 2013). For example, if a household member loses employment, this person's labor supply is often absorbed into a family business (Bridges et al., 2013). While household members can be pushed into entrepreneurship, as growing families (i.e. surplus labor) put pressure on fixed farmland (Reardon, 1997; Reardon et al., 2006; Babatunde and Qaim, 2010), large households may also leverage more resources, such as labor and finance, that in turn facilitate entrepreneurship (Alsos et al., 2013).

Despite the household nature of enterprises, households in rural Africa do not always maximize a single, joint utility function (Ngenzebuke et al., 2014). Instead the decision-making takes place collectively (Chiappori, 1992), either in a cooperative or non-cooperative way (Manser and Brown, 1980). This means that full cooperation might be limited, and that biases against specific household members, for example women, can be expected (Serra, 2009). Female participation might not only be constrained by discrimination in financial and labor markets, but also due to 'rigid social norms' that influence their time-use (Minniti and Naudé, 2010). Nonetheless women have been found to be more likely to engage in the non-farm economy than men (Canagarajah et al., 2001; Rijkers and Costa, 2012; Ackah, 2013).

2.2. Contribution of household income

The vast majority of enterprises are small and informal businesses (Nagler and Naudé, 2014), with 95 percent of rural enterprises employing less than five workers (Haggblade et al., 1989). According to Davis et al. (2014) 44 percent of households in rural Africa participate in the non-farm economy, where self-employment contributes on average 15 percent to household income. 'Farming remains the occupation of choice' with at least 55 percent of household income deriving from agriculture (Davis et al., 2014 p. 26).

Another salient fact is that entrepreneurship in Africa contributes less to household income compared to other regions (Davis et al., 2010, 2014). For instance, Janvry and Sadoulet (2001) find that the non-farm economy contributes on average 55 percent to rural household income in Mexico, whereas Escobal (2001) reports a figure of 51 percent for Peru. Lanjouw and Lanjouw (2001) report 39 percent for Brazil, 41 percent for Chile, 50 percent for Colombia and 59 percent for Costa Rica. Shi et al. (2007) report 46 percent for China.

2.3. Performance

The literature on enterprise performance is largely focused on enterprises in developed economies (see e.g. Moretti, 2004; van Biesebroeck, 2005; Foster et al., 2008; Nichter and Goldmark, 2009; Bloom and van Reenen, 2010; Ali and Peerlings, 2011; Amin, 2011; Kinda et al., 2011; Martin et al., 2011; Saliola and Seker, 2011; Rijkers and Costa, 2012; Bloom et al., 2013). Only a few studies have analyzed enterprise performance in sub-Saharan Africa. These tend to focus either on formal or manufacturing enterprises and are overwhelmingly urban-based. For instance, Frazer (2005), Bekele and Worku (2008), Loening et al. (2008), Shiferaw (2009) and Klapper and Richmond (2011) establish in their work that managerial and technical skills, finance and social networks, the macro-economic and business environment, as well as firm age and size are important determinants of firm performance in urban Africa. Empirical evidence on the performance of rural enterprises is however scarce.

In one of the few existing studies, Rijkers et al. (2010) analyze the productivity of manufacturing enterprises in Ethiopia, and find that rural enterprises are less productive than urban ones. They report an output per labor ratio for remote rural enterprises of 0.43, while it is 0.95 for enterprises in rural towns, and 2.30 for enterprises in urban areas (Rijkers et al., 2010 p.1282). Furthermore they point out that productivity levels are more dispersed in rural enterprises, and that female-headed enterprises are less productive than male-headed ones.

An important dimension of enterprise performance is survival. Although the general view is that rural enterprises face considerable constraints to grow and survive (Bekele and Worku, 2008), only a few empirical studies have analyzed this topic. For instance,

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