



Return to Education for China's Return Migrant Entrepreneurs

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Summary. — This paper examines the return to education for entrepreneurs in rural China with a large return migrant survey dataset. By exploiting the unique culture of male dominance in Chinese society, we use women's education to instrument their husbands' schooling. The results show that the return to one additional year of schooling ranges between 12.6% and 18.8% for China's return migrant entrepreneurs, much larger than the estimated returns to education for off-farm wage workers documented in the literature. We also find that the return to education for entrepreneurs who hire paid workers more than doubles that for own-account workers.
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Key words — return to education, entrepreneurship, self-employment, China, return migration

1. INTRODUCTION

Entrepreneurs are perceived as an important driver of economic growth by contributing many benefits, including incomes, jobs, and innovations, to the society (Djankov, Qian, Roland, & Zhuravskaya, 2006; van der Sluis, van Praag, & Vijverberg, 2008). However, although the labor economics literature (Card, 1999) has extensively studied the return to education for wage earners, little is known about the relationship between human capital and entrepreneurship, specifically, the return to education for entrepreneurs. This paper aims to contribute to the literature by studying the private return to education for China's return migrant entrepreneurs.

According to the human capital theory (Becker, 1964; Mincer, 1974; Schultz, 1961), education can increase individual productivity, and thus lead to more efficient activities. In this sense, education might be able to help entrepreneurs learn and accumulate new knowledge and make good decisions, and thus it contributes to business success (Davidsson & Honig, 2003). On the other hand, the signaling theory (Spence, 1973; Wolpin, 1977) states that education can be used to signal employees' job qualifications to potential employers who cannot explicitly observe their ability in labor markets without complete information. Like employees who are screened by employers, entrepreneurs (especially small business owners) may also be screened by other agents such as customers, capital suppliers, and government agencies. Hence, education is not only acknowledged for its productive effect, but also viewed as a signal of ability for entrepreneurs (Borjas & Bronars, 1989; Parker, 2009). That is, the theories suggest that education plays an important role in entrepreneurial activities as it does for employees.

The related scant literature, however, is mainly about the return to education for entrepreneurs in developed countries.¹ To the best of our knowledge, only several studies (Laszlo, 2005; Smith & Metzger, 1998; Vijverberg, 1995) have examined the return to education for entrepreneurs in developing countries, where the majority of workers are self-employed and entrepreneurial activities provide livelihood for billions of people (Gindling & Newhouse, 2014; La Porta & Shleifer, 2014).² Furthermore, few studies on the return to education for entrepreneurs have accounted for the endogeneity of schooling. It appears to be surprising since doing so is a common practice in the literature regarding the return to

education for employees (van der Sluis, van Praag, & Vijverberg, 2005; van Praag *et al.*, 2013).

As the largest developing country, China is an ideal setting to study the return to education for entrepreneurs. It is commonly observed that some very successful entrepreneurs in China have low education levels, especially those who started their businesses in the 1980s or 1990s when China began to implement its reform and opening up policies (Yueh, 2009; Zhang, Zhang, Rozelle, & Boucher, 2006). Now China is still on its track of transforming from a centrally planned economy to a market economy, and it is argued that other factors such as market opportunities, risk attitudes, and social networks rather than human capital, might be much more important for the success of entrepreneurs (Djankov *et al.*, 2006; Tan, 2001). So, the following question is raised: is formal education important for entrepreneurial performance in transition economies like China?

However, we cannot find the answer to the above question from the literature, despite a growing interest among researchers concerning the return to education for wage earners in China.³ For instance, de Brauw and Rozelle (2008), Heckman and Li (2004), and Li, Liu, and Zhang (2012) all suggest that the return to education for employees has increased since the early 1980s. But how about the return to education for China's entrepreneurs? This issue is arguably more important, as investment in education would be more rewarding due to the positive externality of entrepreneurial activities (Djankov *et al.*, 2006; Fossen & Buttner, 2013; van der Sluis *et al.*, 2008).

This paper examines the return to education for China's return migrant entrepreneurs by using a unique survey dataset. Considering the heterogeneity of entrepreneurs, we also do the empirical analysis separately for own-account workers and entre-

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preneurs who employ paid workers, with the latter group being viewed as more opportunistic and successful. The survey was conducted by the Development Research Center, the State Council of the People's Republic of China to study the entrepreneurial activities of return migrants in rural China. To date, it may be the most comprehensive survey concerning China's rural entrepreneurs, with more than one half of them being returnee entrepreneurs (Démurger & Xu, 2011; Han & Cui, 2007).

The major challenge in our study is how to address the endogeneity of education when studying the return to education for returnee entrepreneurs. The literature typically uses the twins method or exploits exogenous variation in education due to some natural experiments (for example, the staggered rollout of compulsory education laws) to establish the causal relationship between schooling and employees' earnings (Card, 1999; Li *et al.*, 2012; Liu & Zhang, 2013). But the twins datasets on China are not publically available and we cannot find appropriate natural experiments for one's schooling in the setting of China.⁴ In this paper, we exploit China's unique cultural background and use women's education to instrument husbands' education since our main analysis is limited to China's male entrepreneurs. Women's education is arguably a valid instrument in the setting of rural China due to the long tradition of male dominance in the society. Even if the direct effect of spousal education on earnings may exist, it should mainly run from husbands to wives, but not the other way around (Huang, Li, Liu, & Zhang, 2009). Hoogerheide, Block, and Thurik (2012) and Wang (2013) further show that using women's education as the instrument variable in the income regression does not lead to severe estimation bias even if the strict exclusion restriction assumption is substantially violated.

To provide a preview of the main findings, our results show that after accounting for the endogeneity problem, the return to one additional year of schooling for China's return migrant entrepreneurs ranges between 12.6% and 18.8%, much larger than the estimated returns to education for employees documented in the literature. We also find that the return to education for employers more than doubles that for own-account workers in rural China. The estimated return to one year of schooling is between 14.5% and 26.1% for employers, but is only between 4.9% and 8.5% for own-account workers, highlighting the importance of differentiating the two groups when studying the return to education for entrepreneurs.

The main contributions of this paper are at least twofold. On the one hand, it is the first paper to study the return to education for entrepreneurs in China, and it also contributes to the limited literature on the return to education for entrepreneurs in developing countries. On the other hand, this study has accounted for the endogeneity of education, which has been largely neglected in the literature on return to education for entrepreneurs.

The rest of the paper is structured as follows. Section 2 provides the background on entrepreneurial activities in rural China and return migration. Section 3 introduces the survey data used in the analysis, followed by empirical strategies discussed in Section 4. Section 5 presents both OLS and IV estimation results, and explores the heterogeneity of the return to education for return migrant entrepreneurs. The final section concludes.

2. ENTREPRENEURSHIP IN RURAL CHINA AND RETURN MIGRATION

Before China's reform and opening up in late 1970s, individual employment and income were linked to the

commune-based production system and non-agricultural activities were almost non-existent in rural China (Meng, 2012; Zhang, de Brauw, & Rozelle, 2004). Only after the Household Responsibility System was implemented in the early 1980s, have rural laborers been gradually freed from the traditional agriculture to non-agricultural activities, thus promoting the growth of the non-farm sector in China. The share of rural industries represented by township and village enterprises (TVEs) and other rural private enterprises has increased rapidly from 9% to 36% of the national industrial output during 1979–93 (Jin & Qian, 1998). By the end of 2012, the rural non-farm sector employed 138 million workers, representing about one third of the total rural labor force (National Bureau of Statistics of China, 2013b).

The rural enterprises in China usually start off with a small scale and are based on household operation. But they have been increasing markedly and have made great contributions to China's transformation from an agricultural economy to an industrial one (Mohapatra, Rozelle, & Goodhue, 2007; Zhang *et al.*, 2006). According to de Brauw and Rozelle (2008), the self-employed accounted for 16.2% of the total rural labor force, highlighting the possible contributions of rural entrepreneurs to local economic activities. As indicated by Figure 1, the share of non-agricultural income from household business in per capita rural household income has grown steadily from about 2% in 1978 to 12% in 2012, despite the trend of slowing down after 2000 (National Bureau of Statistics of China, 2013a).

Rural–urban migration in China progresses almost at the same pace as the development of rural enterprises. The size of rural–urban migration has grown from less than 16 million in the 1980s to about 166 million in 2013 (Chan, 2001; National Bureau of Statistics of China, 2014). However, due to institutional barriers such as the hukou system, rural migrants have to move circularly between home and cities. Consequently, the majority of them have not been fully assimilated to the way of urban life and cannot settle down permanently in cities (Chan, 2001; Démurger & Xu, 2011; Hu, Xu, & Chen, 2011; Meng, 2012). According to the estimation by Han and Cui (2007) who used the same dataset as we do in this paper, the size of China's rural return migration accounts for nearly one quarter of the total rural migration flow and 10% of the total rural labor force in recent years.

Given the large size of return migration, we can imagine how much returnees could potentially contribute to the development of rural regions in China. As they might represent the flows of both financial and human resources to origin communities (Dustmann & Kirchkamp, 2002; Zhao, 2002),

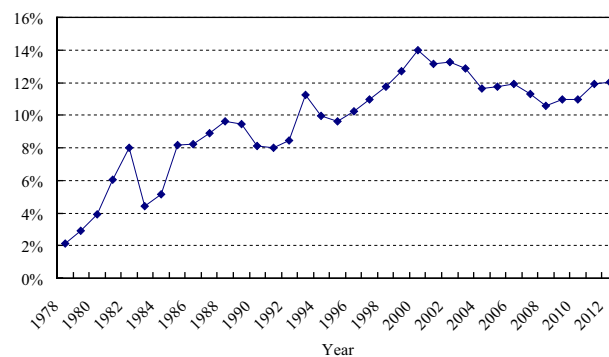


Figure 1. Share of non-agricultural income from household business in per capita rural household income (1978–2012). Data source: China Household Survey Yearbook 2013.

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